

この「日本の税法に関する全般的な解説書」は、2006年4月時点の日本の税制について概説したものです。

本解説書は、もちろん法令ではなく、公定訳でもありません。公的効力を有するのは法令自体であり、あくまでも税制を理解するための参考資料です。この解説書の利用に伴って発生した問題について、一切の責任を負いかねますので、法律上の問題に関しては、官報に掲載された日本語の法令を参照してください。

税制に関するその他の情報については、財務省ホームページ <http://www.mof.go.jp> を御参照ください。

The “Comprehensive Handbook of Japanese Taxes” is an outline of the Japanese tax system in accordance with relevant laws and regulations as of April 2006.

The Handbook is not a law/regulation itself, nor official translation. Only the original Japanese texts of laws and regulations have legal effect. The Handbook is used solely as reference material to aid in the understanding of Japanese laws and regulations. The Government of Japan shall not be responsible for the accuracy, reliability or currency of the legislative material provided in this Website, nor for any consequence resulting from use of the information in this Website. For all purposes of interpreting and applying law to any legal issue or dispute, users should consult the original Japanese texts published in the Official Gazette.

Other detailed information is available on <http://www.mof.go.jp>.

Comprehensive
Handbook
of
Japanese Taxes
2006

TAX BUREAU, MINISTRY OF FINANCE

NOTE TO READERS

Comprehensive Handbook of Japanese Taxes is published annually with the authorization of the Tax Bureau (*Shuzei-Kyoku*) of the Japanese Ministry of Finance.

No rights may be derived from this book. The authors are not liable for any errors or omissions.

[Enquiries]

Write to:

Research Division,
Tax Bureau, Ministry of Finance
3-1-1, Kasumigaseki, Chiyoda-ku,
Tokyo, 100- 0013 JAPAN

CONTENTS

Introduction

Chapter I Introduction to the Japanese Tax System

	Page
1/1 Historical Background.....	1
1. Tax System Before the End of World War II	1
2. Tax System After World War II	3
1/2 Present Tax System.....	18
1/3 Tax Laws and Regulations	21
1. National Taxes	21
2. Local Taxes	26

Taxes on Income

Chapter II Income Tax (Individual Income Tax)

2/1 General.....	27
1. Characteristics of Japanese Income Tax	27
2/2 Taxpayers.....	28
1. Taxpayers and Taxable Income.....	28
2. Rules for Income Attribution.....	30
2/3 Calculation of the Tax Base	31
1. Principles of Taxable Income Calculation	31
2. Categories of Income and Method of Calculation	32
3. Calculation of Business Income	36
4. Special Tax Treatment of Employment Income Deduction for employees specific expenses	40
5. Special Tax Treatment of Timber Income	40
6. Special Tax Treatment of Capital Gains	41
7. Special Tax Treatment of Miscellaneous Income, etc.....	47
8. Nontaxable Income.....	48
9. Aggregation of Income and Treatment of Profits and Losses	50
10. Carryover of Losses	51
11. Carryback of Net Losses.....	52
2/4 Deductions and Exemptions	53
1. Deduction for Casualty Losses	53
2. Deduction for Medical Expenses	53

3.	Deduction for Social Insurance Premiums	53
4.	Deduction for Small-scale Enterprise Mutual Aid Premiums, etc. ..	53
5.	Deduction for Life Insurance Premiums	54
6.	Deduction for Casualty Insurance Premiums	54
7.	Deduction for Contributions or Donations	55
8.	Exemption for the Handicapped	55
9.	Exemption for Widows, Widowers, or Working Students	55
10.	Exemption for Spouses	56
11.	Special Exemption for Spouses	56
12.	Exemption for Dependents	56
13.	Basic Exemption	57
2/5	Calculation of Tax Amounts	57
1.	Tax Rates	57
2.	Averaging Taxation on Timber Income	58
3.	Averaging Taxation on Fluctuating and Extraordinary Income	58
4.	Tax Credits	59
5.	Proportional Tax Credit	62
2/6	Payment of Income Tax	62
1.	General	62
2.	Keeping Proper Records	62
3.	Estimated Payment	63
4.	Final Returns	63
5.	Assessment in the Event of Failure to File Correct Returns	64
2/7	Blue Returns	65
1.	General	65
2.	Approval by the Director of the Tax Office	65
3.	Privileges	65
2/8	Withholding Income Tax at the Source	66
1.	General	66
2.	Interest and Dividend Income	66
3.	Income from Original Issue Discounts on Debentures	67
4.	Employment Income	67
5.	Retirement Income	70
6.	Miscellaneous Income from Public Annuities	70
7.	Remunerations, Fees, etc.	71
8.	Quasi-Financial Products	73
9.	Others	73
2/9	Inquiries and Examinations for Taxpayers and Information Returns	73
1.	Inquiries and Examinations	73
2.	Payment Records	73

Chapter III Corporation Tax (Corporate Income Tax)

3/1	General	76
1.	Characteristics of the Japanese Corporation Tax.....	76
2.	Special Taxation Measures	78
3/2	Taxpayers.....	86
1.	Scope of Taxpayers	86
2.	Rules for Income Attribution.....	88
3/3	Taxable Income	89
1.	Principle of Calculation of Taxable Income	89
2.	Items Excluded from Gross Revenue or Gross Expenses in Calculation of Taxable Income	89
3.	Valuation of Inventories	91
4.	Depreciation Allowance.....	92
5.	Advanced Depreciation	96
6.	Tax-Free Reserves	96
7.	Profit or Loss from the Transfer of Securities and their Term-end Assessment	97
8.	Special Rule for the Recognition of Specific Profits and Expenses ..	99
3/4	Calculation of Tax Amounts.....	99
1.	Methods of Tax Calculation	99
2.	Tax Rates.....	100
3.	Tax Credits	100
4.	Carryover and Carryback of Losses	105
5.	Taxation of retention money on Family Corporations	105
6.	Special Additional Tax on Retirement Pension Funds of Trust Companies, Life Insurance Companies, etc.	106
3/5	Returns Payment, and Refunds of Corporation Tax	106
1.	Final Returns	106
2.	Interim Returns	107
3.	Refunds.....	107
3/6	Blue Returns	108
1.	The Blue Return System	108
2.	Privileges for Corporations Filing a Blue Return	108
3.	Approval by the Director of the Tax Office	108
3/7	Correction and Determination	109
1.	Assessment in the Event of Failure to File Correct Returns	109
2.	Credit of Overpayment of Tax due to Disguised Accounting.....	109
3.	Prohibition of Improper Transaction by a Family Corporation	109
3/8	Special Taxation Measures.....	109

1.	Special tax credit and income deduction	109
2.	Special Measures for Depreciation	112
3.	Reserves	116
4.	Other Special Taxation Measures	119
3/9	Income Examination.....	128
1.	General Investigation Procedures	128
2.	Corporations under the Jurisdiction of the Examination Department	128

Taxes on Property, etc.

Chapter IV Inheritance Tax and Gift Tax

4/1	General	129
4/2	Taxpayers.....	130
4/3	Inheritance Tax	130
1.	Tax Base	130
2.	Basic Exemption	130
3.	Calculation of Tax Amounts.....	131
4.	Tax Rates.....	132
5.	Special Rules for Calculation of the Tax Base with Respect to Small Sites, etc.....	133
6.	Special Tax Treatment for Calculation of Taxable Value for Special Business Assets	134
7.	Special Tax Treatment for Farmland.....	134
4/4	Gift Tax	134
1.	Tax Base	134
2.	Basic Exemption	135
3.	Exemption for Spouses.....	135
4.	Tax Rates.....	135
5.	Special Tax Treatment for Gifts from Parents or Grandparents for Acquiring Residential Properties, etc.....	135
4/5	Taxation System for Settlement at Time of Inheritance	136
1.	Outline	136
2.	Taxpayers covered by this taxation system (His/her age is the age as of January 1 of the year when donation takes place.)	136
3.	Special deduction (range of tax-exemption)	136
4.	Tax amount calculation	136
5.	Application procedures	137
6.	Special cases (applicable till 2006) for acquisition of residence under	

	the taxation system for settlement at the time of inheritance.....	137
4/6	Returns and Tax Payment.....	137
1.	Returns.....	137
2.	Tax Payment.....	137

Chapter V Land Value Tax

5/1	General.....	139
5/2	Taxpayers.....	139
5/3	Tax Base.....	139
5/4	Basic Deductions and Exemptions, etc.....	139
1.	Basic Deductions.....	139
2.	Exemptions, etc.....	139
5/5	Tax Rate	140
5/6	Returns and Tax Payment.....	140

Chapter VI Registration and License Tax

6/1	Taxpayers.....	141
6/2	Taxable Registration and Licenses	141
6/3	Tax Base.....	141
6/4	Tax Rates	142
1.	Registration of Real Estate	142
2.	Registration of Ships.....	142
3.	Registration of Personal Property	142
4.	Registration of Aircraft	143
5.	Registration of Copyrights or Rights of Patent	143
6.	Registration of Commercial Companies	143
7.	Registration of Lawyers, Doctors, Accountants, or Appraisers of Real Property	143
8.	Licensing of Banking Business, etc.	143
9.	Licensing of Manufacture and Sale of Liquor.....	143
10.	Permission for Construction Activities.....	144

Chapter VII Stamp Tax

7/1	Taxpayers.....	145
7/2	Tax Rates	145
7/3	Tax Payment.....	148

General Consumption Taxes

Chapter VIII Consumption Tax

8/1	General	149
8/2	Taxable Items	149
1.	General	149
2.	Transactions subject to Consumption Tax	150
3.	Criteria for Classification of Domestic and Overseas Transactions	152
4.	Non-taxable Transactions	155
5.	Tax Exemption for Exports, etc.	157
6.	Import Transactions	160
8/3	Taxpayers	161
1.	General	161
2.	Base Period	162
3.	Election of Non-Exemption from Tax Liability	162
4.	Special Rules in Cases of Inheritance, Corporate Mergers, and Corporate Division, etc.	163
8/4	Place of Tax Payment	167
8/5	Attribution of Asset Transfers, etc.	168
8/6	Time of Asset Transfers, etc.	168
1.	General Rules	168
2.	Exceptions for Time of Asset Transfers for Installment Sales	169
3.	Exception for Time of Asset Transfers for Construction Work	169
8/7	Tax Base and Tax Rate	170
1.	Tax Base	170
2.	Tax Rate	172
8/8	Tax Credit for Consumption Tax on Purchases, etc.	173
1.	Tax Credit for Consumption Tax on Purchases	173
2.	Adjustment of Tax Deductions on Purchases	176
3.	Simplified Tax System	178
8/9	Other Deductions	179
1.	Tax Deduction for Refunds of Sale Prices	179
2.	Tax Deduction for Losses from ad Debts	179
8/10	Self Assessment and Payment	180
1.	Domestic Transactions	180
2.	Import Transactions	181
8/11	Special Provisions Concerning Government and Entities	182
1.	Special Provisions Concerning National and Local Governments ...	182
2.	Special Provisions Concerning Deductions on Purchases	182

3.	Special Provisions Concerning Due Date for Tax Returns.....	183
8/12	Obligation to Show Gross Price	183

Excise Taxes

Chapter IX Liquor Tax

9/1	General	185
1.	Method of Taxation on Liquor.....	185
2.	Characteristics of Liquor Tax Administration.....	185
9/2	Taxpayers	187
9/3	Tax Base and Tax Rates	187
9/4	Tax Exemption	188
9/5	Assessment and Payment	188

Chapter X Tobacco Tax

10/1	General	189
10/2	Taxpayers	189
10/3	Tax Base	189
10/4	Tax Rates	189
10/5	Tax Payment	190
10/6	Others	190

Chapter XI Special Tobacco Tax

11/1	General	191
11/2	Taxpayers	191
11/3	Tax Base	191
11/4	Tax Rates	191
11/5	Tax Payment	191
11/6	Others	191

Chapter XII Gasoline Tax

12/1	General	192
12/2	Taxpayers	192
12/3	Tax Base	192
12/4	Tax Rate	192
12/5	Tax Payment	192

Chapter XIII Liquefied Petroleum Gas Tax

13/1	General	194
------	---------------	-----

13/2	Taxpayers.....	194
13/3	Tax Base	194
13/4	Tax Rate	194
13/5	Tax Payment	194
13/6	Others	195

Chapter XIV Aviation Fuel Tax

14/1	General.....	196
14/2	Taxpayers.....	196
14/3	Tax Base	196
14/4	Tax Rate	196
14/5	Tax Payment	197

Chapter XV Petroleum And Coal Tax

15/1	General.....	198
15/2	Taxpayers.....	198
15/3	Tax Base	198
15/4	Tax Rates	199
15/5	Tax Payment	199
15/6	Others	200

Chapter XVI Local Road Tax

16/1	General.....	201
16/2	Taxpayers.....	201
16/3	Tax Base	201
16/4	Tax Rate	201
16/5	Tax Payment	201

Chapter XVII Motor Vehicle Tonnage Tax

17/1	General.....	202
17/2	Taxpayers.....	202
17/3	Tax Rates	202
17/4	Tax Payment	205
17/5	Tax Exemption	205
17/6	Other	205

Chapter XVIII Promotion of Power-Resources Development Tax

18/1	General.....	206
18/2	Taxpayers.....	206
18/3	Tax Base	206

18/4	Tax Rate	206
18/5	Tax Payment	206

Payment , Penalties , and Tax Disputes

Chapter XIX Payment of National Taxes

19/1	General	208
19/2	Agencies Collecting National Taxes.....	209
19/3	Budgetary Procedures for Receipt of National Taxes	210

Chapter XX Penalties on National Taxes

20/1	General	211
20/2	Supplementary Taxes.....	211
20/3	National Tax Violation Control Law.....	212

Chapter XXI Collection of National Taxes

21/1	General	213
21/2	Procedure for Collection of National Taxes.....	213
1.	Demand	213
2.	Attachment.....	213
3.	Request for Share Distribution	214
4.	Sale of Properties	214
5.	Distribution of Proceeds, etc.	214
6.	Investigation of a Delinquent Taxpayers Properties	214
21/3	Other Measures to Secure Collection of National Taxes	214
1.	Priority of National Tax Claims	215
2.	Extension of Liability for Tax Payment	215
3.	Advance Collection.....	216
4.	Provisional Attachment.....	216
5.	Provisional Security.....	216
21/4	Protection of Taxpayers and Other Persons Concerned	216
1.	Grace of Tax Payment	216
2.	Properties Not Subject to Attachment	217
3.	Protection of Third Party Rights.....	217
4.	Remedy for Violation of Private Rights	217
21/5	Time Limits on Assessment and Collection	218
1.	General.....	218
2.	Time Limit on Assessment.....	218
3.	Extinctive Prescription of Collection	219

4.	Extinctive Prescription of Refunds	219
21/6	Miscellaneous.....	219
1.	Refund	219
2.	Penalty	219
3.	Interest Tax.....	220

Chapter XXII Tax Disputes

22/1	General	221
22/2	Tax Disputes in the Executive Branch	223
22/3	Tax Disputes in the Judicial Branch.....	225

Local Taxes

Chapter XXIII Local Taxes

23/1	Local Public Entity	226
1.	Legal Foundation.....	226
2.	Kinds of Local Organizations	226
3.	Prefectures	226
4.	Municipalities	227
23/2	Local Public Finance System.....	228
1.	Local Revenue Structure.....	228
2.	Local Taxes	228
3.	Local Transfer Tax.....	229
4.	Special Local Allocation	230
5.	Local Allocation Tax	231
6.	National Subsidies.....	231
7.	Local Public Bonds	232
8.	Miscellaneous Revenues, etc.	232
23/3	Prefectural Taxes.....	232
1.	Prefectural Inhabitants Tax.....	232
2.	Enterprise Tax	234
3.	Local Consumption Tax	238
4.	Real Property Acquisition Tax.....	239
5.	Tobacco Tax.....	240
6.	Golf Course Utilisation Tax	240
7.	Automobile Tax	240
8.	Automobile Acquisition Tax.....	241
9.	Mine-lot Tax	242
10.	Hunting Tax	243

11.	Light–Oil Delivery Tax	243
12.	Other Taxes	243
23/4	Municipal Taxes.....	244
1.	Municipal Inhabitants Tax	244
2.	Property Tax	253
3.	Light Vehicle Tax	254
4.	Tobacco Tax.....	255
5.	Mineral Product Tax.....	255
6.	Special Landholding Tax	255
7.	Bathing Tax	257
8.	Urban Planning Tax.....	257
9.	Business Office Tax.....	257
10.	Other Taxes	258

International Taxation

Chapter XXIV Taxation of Nonresidents and Foreign Corporations

24/1	Taxation of Nonresidents.....	259
1.	Classification of Taxpayers and Their Tax Liabilities	259
2.	Income from Sources within Japan.....	259
3.	Classification of Nonresident Taxpayers and Respective Taxable Income	263
4.	Principle of Tax Calculation.....	265
5.	Special Taxation Measures Applicable to a Nonresident Taxpayer .	265
6.	Withholding Income Tax at the Source	266
7.	Special Rules for Filing a Return and Paying Tax	267
8.	Jurisdiction over Taxation Matters for Nonresidents	267
24/2	Taxation of Foreign Corporations	268
1.	Tax Liabilities—General Rule	268
2.	Income from Sources within Japan.....	268
3.	Classification of Foreign Corporations and Assessment of Corporation Tax and/or Income Tax on Foreign Corporations.....	269
4.	Principle of Tax Calculation.....	271
5.	Withholding Income Tax at the Source	272
6.	Special Rules for Accounting Periods.....	273
7.	Filing of Returns.....	273
8.	Jurisdiction over Taxation Matters of Foreign Corporations	274
24/3	Tax Treaties	274
1.	Japans tax treaties	274

2.	Contents of Treaties	285
----	----------------------------	-----

Administration

Chapter XXV Organization of the National Tax Agency

25/1	General	302
25/2	Tax Bureau of the Ministry of Finance (<i>Shuzei-kyoku</i>)	302
25/3	National Tax Agency (<i>Kokuzei -cho</i>)	303
1.	General	303
2.	Organization	303
3.	Affiliated Organs	305
25/4	Regional Taxation Bureaus (<i>Kokuzei -kyoku</i>)	307
1.	The Management and Co-ordination Department	307
2.	The First Taxation Department	307
3.	The Second Taxation Department	307
4.	The Revenue Management and Collection Department	308
5.	The Examination and Criminal Investigation Department	308
25/5	Tax Office (<i>Zeimusho</i>)	309

Appendix

I	Trends in Tax Reform, etc. in Recent Years.....	312
1.	A Points of the Drastic Tax Reform (December 1988, etc.).....	316
2.	B Points of the Land Taxes Reform, etc.(FY 1991, etc.).....	321
3.	C Points of Tax Reform (November 1994, etc.).....	327
4.	Confirmation of the Consumption Tax Rate (25 June 1996)	331
5.	D Points of Corporate Taxes Reform, etc.(FY 1998, etc.).....	333
6.	E Points of Permanent Tax Reduction, etc.(FY 1999, etc .)	336
7.	FY 2002 Tax Reform (Main Points)	339
8.	FY 2003 Tax Reform (Main Points)	345
9.	FY 2004 Tax Reform (Main Points)	349
10.	FY 2005 Tax Reform (Main Points).....	352
11.	FY 2006 Tax Reform (Main Points).....	354
II	Summary of the National Tax System.....	356
III	Summary of the Local Tax System.....	372
IV	Income Tax Burden	386
1.	Income Tax Revenue	386
2.	Burden of Income Tax and Local Inhabitants Taxes.....	386
3.	Income Tax Threshold	387
4.	Number of Taxpayers and Income for Various Classes of Income (2004)	388
V	Corporation Tax Burden.....	389
1.	Shares of Corporation Tax and Income Tax in Total National Tax Revenue	389
2.	Stratification of Corporations by Capitalization (2004).....	390
VI	Inheritance Tax Burden.....	391
VII	Revenue	392
1.	Revenue from National Taxes; FY 1998 – 2006	392
2.	Revenue from Local Taxes; FY 2003 – 2006	394
VIII	Organizational Chart for the Ministry of Finance	395
IX	Organizational Chart for National Tax Agency (in FY 2005)	396

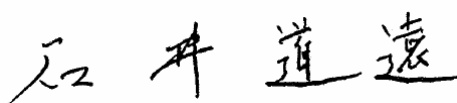
PREFACE

This is the 2006 edition of *Comprehensive Handbook of Japanese Taxes*. We intend to present in this edition a brief sketch of the current Japanese tax system with the most updated information as of April 2006 : changes incorporated in this years' edition are amendments to tax laws and regulations enacted in FY 2005 (from 1 April 2005 to 31 March 2006).

In addition to this brochure, the latest information can now be obtained on the Internet where our address is: <http://www.mof.go.jp>.

Hopefully, this edition will help readers worldwide obtain a better and thorough understanding of Japans tax system.

Tokyo, November 2006

A handwritten signature in black ink, consisting of four characters: 江, 井, 道, 遠 (Ishii Michito).

Michito Ishii
Director-General, Tax Bureau
Ministry of Finance, Government of Japan

CHAPTER I

INTRODUCTION TO THE JAPANESE TAX SYSTEM

1/1 Historical Background

1. Tax System Before the End of World War II

(1) Prior to the Beginning of World War II

A modern tax system was established in Japan approximately 20 years after the Meiji Restoration (1868), when Japan emerged from feudalism. Until that time the Japanese tax system had relied mainly upon land taxes, which represented more than 80% of all tax collected. Rapid development of a capitalism economy in the Meiji period brought about broad changes in the tax system. An income tax system was introduced in 1887, making Japan one of the first countries to adopt an income tax system with modern features. However, since economic development was still at an early stage, income tax played only a minor role in total tax revenue (1.5% in 1888); the number of people paying income tax was only 118,600 out of a total population of 39 million, while land tax still accounted for more than half of the aggregate tax revenue (53.8% in 1888). As the modern tax system developed in Japan, the importance of land tax for revenue decreased steadily. This trend continued until 1940, when the income tax system was expanded and the indirect tax system was modernized.

Supported by an increase in national income and improved administration, the income tax system gradually evolved: provisions of the tax law were more precisely defined, the number of taxpayers increased, tax revenue grew gradually, and the importance of income tax in national finance increased. Until 1908, land tax was the main source of national tax revenue. Indirect taxes, of which the liquor tax was the most important, expanded gradually. Since 1935, income tax has been the most important single item in tax revenue. Major changes up to World War II included:

Year	Major Tax Reforms	Descriptions
1868 Meiji Restoration 1872	Reform of land Tax (land tax revenues accounted for more than 80% of total tax revenue)	The tax base changed from crops to the value of the land. A fixed tax rate was applied. Payment in cash was adopted in place of payment in kind.

Introduction to the Japanese Tax System

Year	Major Tax Reforms	Descriptions
1887	Introduction of an income tax system	A general income tax as levied on the aggregate income of each individual, the level of basic exemption being 300 yen and progressive rates ranging from 1% to 3%. Individuals paying income tax in 1887 numbered about 120,000.
1889 Promulgation of the Meiji Constitution		
1894 Sino-Japanese War		
1896	Introduction of a registration tax and business tax and the reorganization of tax collection organs	Business tax as imposed on the capital amount, and the number of employees, etc. 504 district tax offices were established.
1899	Introduction of scheduler income taxation, including corporate income taxation and with holding tax on interest	Income tax as divided into three schedules; I (e.g., corporate income, tax rate 2.5 %), II (e.g., interest, tax rate 2%), and III (e.g., personal income, tax rates 1%~5.5%). Income tax was not imposed on dividends received by individuals, thus avoiding double taxation of income from dividends.
1904 Russo-Japanese War		
1913	Introduction of an employment income deduction	10% of employment income as deductible Tax rates ranging from 2.5% to 22%.
1914 World War I		
1920 Establishment of the League of Nations	Introduction of exemption for dependents and withholding tax system for some income categories	Interest on term deposits and dividends and bonus payable to nonresidents became subject to withholding tax. Exemption for dependents as 50 or 100yen for each dependent according to the taxpayer's income. Dividends received by individuals, less a 40% deduction, were included in taxable income. Tax rates ranged from 0.5% to 36%.
1921 Limitation of Armaments Conference		
1926	Tax reform for both national and local tax systems	A business profits tax was introduced as a supplement to income tax, replacing business tax. The land tax base was changed from the price to the rental value of the land. The indirect tax system was reorganized.
1932 Shanghai Incident	A series of tax increases to meet increased fiscal needs and the introduction of commodity tax	
1939 World War II		

(2) Tax System during World War II

A. Direct Tax System

In 1940, overall reform of the tax system was carried out to meet the requirements of the wartime economy and to refine the tax system as a whole. The main characteristics of this reform were as follows:

- a. The direct national tax system was rearranged. The former income tax was levied not only on individuals but also on corporations. The new income tax, as a rule, applied only to individuals, and consisted of two parts; namely, a scheduler income tax and a comprehensive income tax.
- b. With the scheduler income tax, income was divided into six schedules according to the nature of income; i.e., (i) real property income, (ii) dividends and interest income, (iii) business income, (iv) employment income, (v) timber income, and (vi) retirement income. Different rates were used with each schedule in calculating income tax liability. The idea of a basic exemption was introduced for business income and employment income.
- c. Comprehensive income tax on aggregate income was imposed at progressive rates (10%~65%).
- d. With respect to corporate income, the Corporation Tax Law was introduced. Corporate income was taxed at the rate of 18%.
- e. With respect to employment income, withholding tax at a flat rate of 6% was introduced.

B. Indirect Tax System

Main reforms of the indirect tax system during this period involved:

- a. After 1938, the number of commodities that were subject to the commodity tax increased and rates were differentiated according to commodity.
- b. The liquor tax, which had been the leading item of indirect taxes, was simplified in 1940.

C. Increased Role of Direct Taxation

As a result of the tax reform of 1940, Japan's tax system came to rely mainly on direct taxes. The share of direct taxes, 67% of which was income tax and corporation tax, reached 64% of total tax revenue in 1941.

2. Tax System After World War II

The history of the Japanese tax system was characterized by the influence of

the United States for more than 30 years after World War II, and especially the philosophy of Professor Carl S. Shoup's recommendations; later modification of the tax system was made in an effort to adapt it to Japanese society. Since by its nature taxation is closely connected with economic and social conditions, the modification and development of the Japanese tax system mentioned also reflected changing circumstances in Japan prior to its present economic status. From this point of view, the postwar history of the Japanese taxation system can be divided into four periods: the first period when the economy was in chaos (1945—49), the second period featuring economic reconstruction (1950—59), the third period marked by the achievement of economic growth (1960—69), and the fourth period devoted to the improvement of national welfare (1970 to the present).

(1) First Period - Economic Chaos after the War (1945 - 49)

The war left the Japanese economy in shambles, ravaged by rampant inflation. The goal of fiscal policy at the time was simply to cope with this crisis in the nation's economy. Many reforms were undertaken so as to coordinate tax policy with other economic policies. For example, a special tax on war indemnity was introduced for the purpose of canceling various claims for compensation.

A. Introduction of Anti-inflationary Tax Measures

One of the anti-inflationary measures introduced in 1946 was the property tax, which was also designed to redistribute national income. Since the Japanese people were forced to deplete their contingency reserves after the end of the war, the new tax did not prove fully effective in curbing hyper-inflation. However, this new tax substantially redistributed income through its extraordinarily progressive tax rates ranging from 25% to 90%.

Another special tax for wartime compensation newly introduced was to be levied on wartime compensation of munitions companies, etc. at 100%. This tax was contrived to put an end to the obligation claimed against the government for wartime compensation by munitions companies, etc.

B. Introduction of the Self-assessment System on a Current Basis

The dual income tax system, in effect since 1940, was abolished in 1947, which made it impossible to secure adequate revenue through conventional means. A new method was adopted to permit a taxpayer to assess his or her own income tax on the basis of income for the current year. Previously, income tax on such categories of income as earnings from business and agriculture had been generally assessed by tax officials on the basis of a taxpayer's income in

the preceding year. However, the implementation of this new system met with a storm of opposition from taxpayers because it was considered a radical change in the method of taxation. In order to collect the amount of taxes due, the government had to embark on sweeping countermeasures immediately after the final reporting period.

C. Trial Introduction of the Turnover Tax

One of the remarkable events in taxation during this period was the introduction of the turnover tax and its abrogation. This tax was levied on the basis of the sales amount at every stage of a transaction at the rate of 1%. Its aim was to flexibly meet revenue needs according to economic changes. Collection was first made by the sale of stamps to vendors, but this method produced numerous complaints from taxpayers. It was later changed to collection on the basis of a return submitted monthly by the taxpayer. The enforcement of the tax required close examination of taxpayers' accounting books, which made the tax very unpopular. It was also argued that this tax dealt a hard blow to small businesses, which could hardly afford to shift the tax burden to consumers. The ill-fated tax was abolished in 1950, following suggestions made by the Shoup Mission.

D. Local Tax System

In 1947 and 1948, the local tax system was reviewed. In order to establish a sound local financial system, administration of several national taxes such as the land tax, house tax, business tax, mineral product tax, and amusement tax were transferred to local governments.

E. Establishment of National Tax Agency

One of the notable changes in the field of tax administration was the establishment of the National Tax Agency in 1949. The reorganization of tax administration was intended to allow the government to enforce tax laws more efficiently and to clarify the authority and responsibilities of the tax administration by reallocating these functions of the Tax Bureau of the Ministry of Finance.

(2) Second Period - Economic Stabilization and Restoration (1950 - 59)

Since the late 1940s, stringent economic policy was pursued in accordance with the plan worked out by Dr. Joseph M. Dodge, then advisor to the General Headquarters, who pointed out that the maintenance of a balanced budget was necessary to halt inflation. In the same year, a mission headed by Professor Carl S. Shoup was invited to review the structure and administration of the Japanese

tax system. After four months' study of the Japanese tax system, the Mission submitted recommendations for an overall tax reform plan, which was incorporated in the 1950 tax reform.

A. Main Features of the Reform of 1950 based on the Shoup Recommendations

Professor Shoup's approach placed direct taxes, and especially income tax and corporation tax, at the centre of the entire taxation structure. In theory, income tax was to be complemented by a net wealth tax and on inheritance tax. For corporation tax purposes, a corporation was deemed to be a mere aggregate of shareholders not constituting an independent taxable entity.

It is to be noted that a system called the "blue return system" originated from Professor Shoup's recommendations. This system involved a basic over-haul of the administration of the income tax system.

a. National Taxes

(a) Introduction of a new concept for the corporation tax

The most important issue in the income tax field was the introduction of a concept that the corporation tax was an advance payment of individual income tax by shareholders. In order to avoid double taxation, dividends received by a corporation were exempt from corporation tax and a 25% credit with respect to income tax was granted for dividends received by individuals.

At the same time, a corporation tax of 2% was levied on undistributed profits on the grounds that the holding in reserve of profits by a corporation amounted to the deferral of shareholders' personal income taxes.

(b) Overall aggregation of income

The principle of aggregation of income was applied to all categories of income, including temporary income. Income derived from securities transactions and all other income derived from the transfer of assets (capital gains) was now subject to the income tax.

(c) Revaluation of assets

On the other hand, the fall in the value of currency due to rapid inflation caused a substantial difference between the current value and the book value of fixed assets. To make the capital structure more realistic, a revaluation of assets was undertaken. Revaluation of assets for business use was optional, while revaluation of other individual assets was obligatory at the time of transfer for such assets. A surplus arising from revaluation was treated as if it had accrued from the transfer of properties, but such income was taxed at a reduced flat rate of 6%.

(d) Introduction of a net wealth tax

Coupled with the lowering of the maximum income tax rate from 85% to 55%, a net worth tax was supplementarily levied on persons with large incomes from property.

Individuals whose net assets exceeded ¥5 million were taxed at progressive rates, ranging from 0.5% to 3%, according to their net wealth.

(e) Others

Widespread special taxation, though given on the pretext of economic and industrial needs, had undermined basic tax principles. In the reform of 1950, special measure was reduced to the practical minimum.

b. Local Taxes

(a) Granting of an independent right of taxation to each local entity prefectures previously levied such taxes as the land tax, house tax, enterprise tax, and consumption tax on hotels and restaurants, while the financial resources of municipalities were provided by a surtax on these taxes. This system was abolished in 1947, and all local entities were given an independent right to tax.

(b) Enactment of a value-added tax

A new law was enacted in 1950 to introduce a value-added tax on production or marketing under the local tax system. The tax base of the value-added tax was the gross receipts of an enterprise less its purchases from other enterprises; consequently wages payable to its employees as well as interest and rent payable to other firms were included in the base. This proposal was immediately criticized because enterprises employing large labor forces would be penalized. There was also a strong sentiment among businessmen opposing a tax that must be paid by an enterprise even when its operations resulted in a loss. For these and other reasons, opposition to the new tax was vehement. The controversial law was later revised to a slight degree. Enforcement of the law was postponed several times, but it was finally repealed in 1954 without having been put into operation.

B. Modifying Shoup's Taxation System

a. In general, the tax reforms based on the recommendations of the Shoup Mission of 1950 sought an optimal long-term tax system. The mission's intentions, however, were somewhat idealistic and did not consider the reality of the Japanese economy and the standard of living for the Japanese people. Yearly tax reforms since 1951 represented an effort to re-adjust the tax system to meet actual conditions prevailing in the country.

b. The following brief review of a series of tax reforms since 1951 shows the

process of modification through which the tax system based on the Shoup recommendations was adjusted.

(a) Abolition of taxation on the retained profits of corporations

For the purpose of the corporation tax, retained profits at the end of each accounting period had been taxed at the rate of 2%, in line with the suggestion by the Shoup Mission that such tax be deemed an interest surcharge on retained profits. However, in light of the important role of profit retention in business financing, the retained profit taxation of corporations other than “family corporations” was abandoned in 1952.

(b) Abolition of taxation on capital gains derived from the transfer of securities

The philosophy of the Shoup recommendations was to make all categories of income, including capital gains, subject to individual income tax. However, in 1953, capital gains from the transfer of securities were made non-taxable, not only because the taxation of capital gains allegedly hampered the development of the securities market, but also because taxes on such gains were technically difficult to assess and to collect.

(c) Abolition of the net wealth tax

The net wealth tax proved inequitable because real property owners whose net wealth is easily identified bore the full brunt of taxation while others avoided the burden to an extent. Consequently, this tax was abolished in 1953.

(d) Measures for the development of the Japanese economy

The Shoup recommendations were founded on the general principle of equitable sharing of the burdens to meet government expenditures, avoiding arbitrary reduction of the tax burden even at the cost of economic policy goals. A number of concerned persons in the government, however, felt that in light of the prevailing condition of the Japanese economy, vital economic policies might override certain general principles of taxation. As a result, several measures were initiated in 1953 to this end, including the extension of special depreciation allowances, wider application of reserves for bad debts and price fluctuations, exemption of certain income from exports, and other provisions.

(e) Transformation of the death tax

On the basis of the Shoup recommendations, the death tax was transformed from the former estate tax system into an inheritance tax system. The results were unsatisfactory because the tax amount due varied depending on the method of dividing the estate. Taxpayers often made false reports of the amount received. In 1958, revision was made to calculate the tax on the basis of the statutory shares of estates provided under the Civil

Code.

C. Natural Increase in Revenue and the Adjustment of the Tax Burden

- a. Reduction of direct tax commensurate with economic development The latter half of the 1950s saw remarkable development of the Japanese economy, and the increase in tax revenues resulting from economic expansion was so great that the idea of reducing direct taxes was felt to merit study. Annual tax revisions since 1951 were designed to raise the basic exemption and the exemption for dependents and employment income exemption, while also making income tax less progressive as revenues increased due to rapid economic development.

- b. Establishment of the Tax Commission

Since the end of the war, the principle of budgeting had been to draft the budget solely in relation to tax revenues. However, increasing tax revenues due to high economic growth in the period necessitated that the government fundamentally review the tax system in order to maintain the equitable sharing of the tax burden and to adapt the current tax system to new economic conditions.

To meet these requirements, a Tax Commission composed of economists and other experts in various fields of society was established in 1959 as one of the advisory organs to the Cabinet. Since that time, yearly tax amendments have largely been based on reports submitted by the Tax Commission.

(3) Third Period - Economic Progress (1960 - 69)

A. Pursuit of Tax Reduction Policies and Refinement of the Taxation System

- a. In 1959 the Tax Commission was directed to find ways to improve the tax system and divide tax revenue between national and local governments on a reasonable basis. Major tax questions at the time concerned the taxation system in general, taxation of business enterprises, and sharing of government revenues.

After examining the present tax burden in comparison to that of the prewar period and those in foreign countries, and in relation to budgetary expenditures and similar items, the Tax Commission submitted the first report in 1960 estimating that the tax burden should be limited to approximately 20% of national income. Expectations were that the ensuing national and local tax burden would be around 20% and that a part of any unexpected increase in revenues resulting from economic growth would be used as a resource to reduce taxes each year.

- b.** Thus, throughout this period, one major tax policy was a series of tax reduction programs, in accordance with the recommendations of successive Tax Commissions, which all insisted on a lessening of the income tax burden.

At the same time, as a result of yearly reductions in the burden of direct taxes, indirect taxes came to be increasingly levied even on the taxpayers who are exempted from paying income taxes. Thus, the Tax Commission recommended in 1961 that the rate of indirect tax should be, in principle, approximately 10% of consumer prices or 20% of producer prices.

- c.** Accompanying this tax reduction policy was the refinement of tax laws. In the second report issued in 1961, the Tax Commission recommended the enactment of a general law for national taxation establishing general and fundamental principles of taxation such as the principle of substantial taxation, limit to the period of tax claims, method of taxation procedures for the self-assessment and imposition, obligation of bookkeeping, authority to inquire and inspect, additions to taxes, notification procedure tax disputes, penalties and rule-infringement control. As a result of the report, the General National Tax Law was enacted in 1962. Another significant improvement was the introduction of the self assessment system for indirect taxes, following the recommendations of the Tax Commission.

B. Long-range Plan for Taxation

The Tax Commission was requested by the Prime Minister in 1962 to study the ideal way that the fundamental system of taxation should be adjusted to match the future progress of the national economy and society. In 1964, the Tax Commission presented its final report after three years of intensive study, intent on examining the present taxation system and providing perspectives for future tax reform so that further economic growth might be achieved under the government's trade liberalization policy. The main points cited by the Tax Commission were:

- a.** New criterion for tax reduction

The Tax Commission introduced a new criterion for tax reduction; namely, the amount of tax reduction in the next several years should be around 20% of the expected annual increase in tax revenue under the existing taxation system. Since the increase in tax revenue would be substantial with rapid and sustained economic growth, determining an appropriate division of this added revenue into tax reduction and increased public expenditures became of vital importance.

- b.** Importance of income tax in the overall taxation system

Income tax: (a) is a suitable means to distribute resources for public purposes since it can bring sufficient revenue without impacting the market price

mechanism; (b) can perform its function best to redistribute incomes through progressive structure combined with deductions and tax rates and; (c) retains a good function to stabilize business conditions with its highly elastic tax revenue and its action as built-in-stabilizer. Consequently, income tax is the most modernized tax and the tax system is ideal in which, income tax plays the central role. However, in consideration of the present situation of the tax burden etc, future tax reduction should concentrate on income taxes as before since it will be necessary to reduce and rationalize the tax burden in correspondence with increase in incomes and living standards throughout the nation.

c. Abolition of special taxation measures

Special taxation measures are significant as a part of economic policies to utilize tax incentive effects as a means to attain their certain purposes. However, in consideration of their demerits such as hindrance to the principle of the equity of tax burden and the neutrality of taxation which may harmfully impact the morality of taxpayers, streamlining them should also be facilitated from now on.

In particular, special taxation measures on asset income such as those on interests and dividends should be abolished since they may give much evil influences through exceedingly favorable treatment of some high asset income owners and it is difficult to demonstrate any political effects as a compensation for the demerit.

d. Tax withheld at corporation level on dividends

With regard to the tax reduction for dividends adopted in 1961, since no effect was noted on promotion of capital increase which the system was aimed at, and the system became increasingly complicated through joint use of the tax reduction for dividends and the dividend tax deduction, it will be appropriate to adopt a tax withheld at corporation level on dividends.

C. Tax System Pursuant to Deficit Financing Policies and the Issue of Government Bonds

- a.** Japan's economy made an unprecedented rapid growth during the 1950s. With the rapid growth and the progressive taxation structure, tax revenues were extended to renew the record of economic growth rate by a considerably high rate almost every year. With the above as a back-ground, it was possible for Japan's financial situation to appropriate most of the natural growth of tax revenues to the increase in expenditures, tax reductions with a part of the natural growth of tax revenue, and it was still possible to appropriate not a little amount to a surplus fund. In the meantime, the preconditions for the tax policy were maintenance of these economic trends and the

principle of balanced financial conditions.

However, tax revenue marked little increase during the period of stagnation from 1964 to 1965, and this led to a new situation of issuing governmental bonds to cover the loss of revenue for the supplementary budget of FY 1965. Then in FY 1966, the government decided on the full scale issuance of governmental construction bonds. From the aspect of taxation, the financial policy was positively converted including enforcement of tax reduction largely in excess of the estimated natural growth of tax revenue, thus, giving a remarkably overcoming depression in some way or other. Thus, the importance of financial affairs to ensure a stable economic growth came to be recognized more than before. It became also necessary to review from a new angle the way a tax policy should be.

- b.** With respect to this matter, Tax Commission released the interim report and the final report in 1966 and 1968 respectively. The basic idea of the final report was that the existing fundamental structure should be retained. The main points noted in the report were:

(a) Direct taxes

With respect to the income tax, the tax threshold should be raised to approximately one million yen for an employment income earner with a spouse and three children and, at the same time, necessary improvements should be made for employment income deductions and tax rate structure.

As for the corporation tax, while the fundamental review of the basic scheme should be continued for the time being, effective and appropriate measures should be taken to cope with the urgent request for intensified international competitiveness of corporations.

(b) Indirect taxes

Taking their relationships with prices into consideration, targets of taxation and tax rate structures should be reviewed from time to time so that they may be adaptable to changes in economy and society, especially to changes in the style of consumption. At the same time, efforts should be made to maintain the appropriate level of indirect tax burdens for both individual articles and overall consumption expenditures within the limit of possibility.

(c) Other items

It is necessary to improve the present appeal system for the settlement of tax disputes and to reform the taxation rules related to land.

(4) **Fourth Period - Improvement in National Welfare (1970 to the pre-sent)**

A. Growing Role of the Public Sector

For 25 years after World War II, the Japanese economy grew steadily, giving Japan the second largest gross national product (GNP) in the free world and a comfortable balance-of-payments position. At the same time, however, the rapid economic growth of the past brought to the fore the relative lack of infrastructure. In order to fulfill the urgent task of correcting various distortions in the Japanese economy such as environmental pollution and the need to improve the quality of life, the economy had to shift from one spearheaded by investment in the private sector to one led by public finance.

B. Restoration of the Fiscal Balance

Reflecting the severe recession after the oil crisis, however, tax revenue stagnated markedly in FY 1975 and a large issue of “deficit-financing bonds” was needed to cover the revenue shortfall. Tax revenue did not recover from this stagnation and the ratio of bond issues to total expenditures in the national budget continued to be extraordinarily high from 1975 on, reaching 34.7% (with bond issues amounting to ¥13.47 trillion) in FY 1979. Of the ¥13.47 trillion worth of national bonds issued in FY 1979, ¥7.13 trillion were construction bonds appropriated for capital expenditures and the remaining ¥6.34 trillion were deficit-financing bonds appropriated for current expenditures.

Fears were that a continuation of these irregular conditions, in which budget financing depends on a large issue of national bonds and especially deficit-financing bonds, might disturb the healthy development of the national economy. Thus, reducing the budgetary deficit became an important national goal. Drastic efforts have been made to economize and rationalize expenses, and the scale of expenditures as a whole has been strictly curtailed, by limiting general expenditures other than those for national bonds as much as possible and by the distribution of local allocation taxes. Consequently, the annual growth rate of expenditures with respect to the initial budget for the previous fiscal year has been severely limited.

Secondly, in terms of the tax system, a growing number of special taxation measures have been curtailed or repealed since FY 1976. At the same time, taxable objects, tax bases, and tax rates of existing taxes have been re-examined. As a result, tax increases in FY 1981 covered a broad range, including corporation tax rates, liquor tax rates, stamp tax rates, and other items.

(5) Recent Tax Reforms

A. Drastic Tax Reform of 1987 to 1988

The high economic growth and two oil crises led to drastic changes in Japan's economic society. Out of structural changes such as increase in standardized income levels, diversified consumption and greater consumption of services, aging of population structure and globalized economic transactions, various issues on the conventional tax system based on Shoup's Advice were presented and a drastic tax reform took place from 1987 to 1988.

- a. Looking over the tax systems before the drastic tax reform, around 1975 when the high economic growth and frequent tax reductions were over no review was made on the personal income tax system and taxation came to largely depend on income taxes. Since taxpayers felt they were being burdened with higher tax payments due to considerably strong progressiveness in personal income taxes and an imbalance of collection among different types of incomes interest in guaranteeing the equity of tax burden is greater than ever.

Unlike other leading countries, Japan's consumption tax had long depended only on indirect taxes centering on commodity taxes levied on individual commodities for their luxury and convenience, and this caused an unbalanced taxation of individual commodities. In addition, since services had not been targets of taxation, it was impossible to cope with the changes revealed in the issues of diversified consumption and greater consumption of services, resulting in serious problems from the viewpoint of maintaining equity, neutrality and simplicity of tax systems.

Moreover, since the full-scale aged society with a smaller number of children is coming in the near future, the conventional taxation system was considered as unsuitable for creating of a richer economic society. This might cause an increased burden for the working generation whose numbers would be relatively smaller compared with that of the aged generation, resulting in less willingness to work and create business activities. Therefore, it was necessary to construct a tax system to enable more people to support their society and ensure a stable revenue system to fill the increasing financial needs such as social security.

- b. Based on these circumstances, with personal income tax continuously ranked as the core of the tax system, a large-scale tax reduction should be done, so that they will be more willing to work and create business activities. Therefore, mitigation and simplification of progressive tax rate and a review on various deductions were made. As for income from assets, rationalization of taxation was realized through reviews of taxation of interests and capital

gains from stock transfer to ensure equity of taxation. As for taxation of corporations, tax base was broadened and the effective tax rate was reduced by differing emphasis on equity of tax burden, economy activation and simplicity of taxation.

With respect to the consumption tax, equity of the real tax burden should be realized throughout the entire tax system. Moreover, to help stabilize the revenue structure required for providing public services which has been increased as society ages it was considered as necessary to seek for wide-ranged and equal tax burden based on general consumption. The conventional, indirect tax system where taxes were imposed only on limited commodities and services should be drastically revised, and a possibility should be examined for foundation of sales tax imposed on the general consumption. The bill of this new tax was abolished although it was introduced in the Diet in 1987. Afterwards, streamlining individual indirect taxes and the foundation for a consumption tax were examined based on the insistence and discussion made concerning sales taxes, and the Law on Tax Reform including reform of the indirect tax system was enacted in December 1988. Consumption tax was also realized in April 1989.

As for inheritance tax and donation tax, no review had been made on them since 1975. Therefore, measures were taken to raise the tax threshold and mitigate tax progressiveness to ensure reduction in the tax burden and rationalization of the tax system.

B. Tax reform from 1989

a. Tax reform of 1994

This reform was enforced from the standpoint that the leveling of tax burden throughout generations would be important for all members of society in accordance with the basic principles of equity, neutrality and simplicity so that the working generation supporting the aged society with smaller number of children may not suffer from excessive and imbalanced tax burden, and the society of fair and active welfare may be realized. With the enactment of the related law in November 1994, the tax reform was realized from the viewpoint of creating a tax system where taxpayers are willing to pay their fair share. To be specific, the personal income tax was largely reduced through mitigation of the entire progressive tax rate structure so that the sense of being under increased tax burden might be mitigated centering on the middle income earners. As for consumption tax, necessary reviews were made on special measures for medium- and small sized enterprises so that tax burden might be widely shared by the members of society. The tax rate was raised to substantiate the consumption tax system and local consumption tax was es-

established.

The tax reform of 1994 was to cope with the structural changes in economy and society. At the same time, this reform had another aspect of stimulative measures. In other words, in consideration of the economic situation, increase in the rate of consumption tax rate was to be implemented in April 1997 in parallel with the institutional reduction in personal income taxes for FY 1995 and onward combined with the special tax reduction for FYs 1994 to 1996. Thus, a precedent tax reduction was realized.

As for inheritance tax, to contrive to simplify the system and to mitigate the increase in the average tax rate, the tax threshold was raised and the range of brackets was enlarged.

b. Land taxation system

With what is called the “land mythology” as a background, the Basic Land Act was enacted with the basic idea of maintaining ownership of land for the common good aimed at promotion of the general land policy involving review of the land tax system. From 1991 to 1992, the land tax system was reformed to rationalize taxation of capital gains from land transfer and establish the land value tax. This reform was based on the viewpoints of appropriate and fair sharing of the tax burden and land policy to create effective use of land while decreasing the profitability of land as a property and controlling land speculation. Afterwards, reduction in tax burden was realized in response to the land value decline and stagnation. In 1998 the land value tax was suspended and through revision of the taxation on capital gains from land transfer from 1995 FY to 1999 FY, the tax burden was lowered than that during the “bubble economy (in latter half of 1980s and early in 1990s).” Because of the soaring land price in the bubble period, inheritance tax has been cut continuously since 1988. With the slump of land price after the bubble period, the tax burden of inheritance tax have been lowered greatly.

c. Financial taxation system

With the progress of financial liberalization and internationalization, it was inevitable for Japan’s financial system to enforce a remarkable reform in order to create competitive market. In response to such reform of the financial system, necessary tax measures were timely taken. For example, to correspond with the liberalization of the foreign exchange system in April 1998, the system to submit reports on remittance abroad was established, and tax measures were taken on SPC and stock options. In the tax reform of 1999, accompanying rationalization of capital gains from stock transfers, Securities Transaction Tax and Bourse Tax were abolished. Moreover, from the standpoint of helping the internationalization of the yen, measures were taken to exempt nonresidents from withholding at the source of the interest

concerning national bonds for lump sum registration and TB/FB issuance in addition to the collateral measures alternative to tax rationalization.

d. Corporation taxation system

No general review of tax base was made since 1965 when the Corporation Tax Law was entirely revised. However, the corporation tax system was reformed in 1998 both on the tax base and tax rate. Through this reform, the tax rate of reserves and depreciation were rationalized and effective tax rates were lowered for corporation taxes from the viewpoint of ensuring the vitality and international competitiveness of companies through promotion of tax neutrality for economic activities.

C. Recent counter - cyclical policies and permanent tax reduction

Because of the impact of the currency crisis in Asia and the successive failures of financial institutions, Japan's economy has been in an extremely serious situation since autumn of 1997. The serious situation lasted with minus 0.1% as the real growth rate of GDP for FY 1997, which was the first minus growth since 1974 and also minus 1.9% for FY 1998, the following year. From the standpoint of ensuring business recovery, countermeasures were required through use of every possible financial and monetary measure. Since utmost consideration was required also for the tax system, special tax reduction was effected twice in FY 1998 on the personal income tax. In the tax reform of FY 1999, based on the opinion that tax reduction only for a year would be insufficient, tax reduction was effected in the largest scale on personal income tax and corporation taxes to cover the amount considerably in excess of ¥6 trillion. This tax reduction has been continued up to now. As a part of this permanent tax reduction, reductions were realized in the highest bracket of personal income tax and in the effective tax rate of corporation tax to be similar to the international level. As stated above, the permanent tax reduction includes partial tax reduction anticipating the direction of a drastic reform to be enforced in the future. However, based on the business conditions of the time, only the measures to realize tax reduction were enforced. Review of tax base, etc. of personal income tax and corporation tax still remains as an issue to be examined in the future.

D. Tax reform toward the construction of a desirable tax system

Now that the 21st century has begun, the structure of the Japanese socio-economy is changing greatly because of the rapidly aging society and married couples having a smaller number of children, diversified life styles and globalization of the country. To sufficiently respond to these various structural changes and to realize sustainable activation of the socio-economy, it is considered necessary to execute reform toward the construction of a desirable tax

system based on medium to long-term viewpoints.

In the tax reform in 2003, the first step of the reform toward the construction of “a desirable tax system” on corporation tax should be taken so that a sustainable socio-economy may be activated. Inheritance and gift taxes should be unified to achieve integration. Thus, measures such as the increased tax reductions for R&D and investment in plant and equipment to support growth of strategies to innovate in the 21st century and unification of the inheritance and gift taxes to help smooth transfer of assets to the next generation are taken. Further more, taxation of financial assets and securities should be comprehensively reviewed to help the reform “from saving to investment,” distorted tax burdens should be corrected and tax burdens should be fairly shared by all the people. From these viewpoints, a wide-ranging reform was made as a package including abolition of the special tax deduction for spouses (additional part) on personal incomes and reduction of special measures for small and medium-sized corporations aimed at promoting the solidity and transparency of consumption tax.

In the FY2006 tax reform, in a continuous effort to implement a “desirable tax system,” a major transfer of sources of tax revenue in personal income taxes from the individual income tax to inhabitants taxes, amounting to 3 trillion yen, was conducted as part of the trinity reform. Also the proportional tax credit, which had been in place since 1999 as a temporary and exceptional measure to boost the economy, was abolished in light of the economic recovery. In corporation taxes, R&D-related taxation was revised to promote private research and development activities, and a new tax system was established to strengthen the information infrastructure and to increase competitiveness. Additionally, other wide-ranging revisions were made, including the simplification of liquor classification, narrowing of the differences in tax rates among liquors and the abolition of public announcement of taxpayers who have paid large amount of taxes.

1/2 Present Tax System

Current taxes levied by national and local governments in Japan can be classified into three groups: taxes on income; property, etc. ; and consumption.

1. Taxes on Income:

National Taxes Income Tax (Individual Income Tax) and Corporation Tax (Corporate Income Tax).

Local Taxes Prefectural Inhabitants Tax, Municipal Inhabitants Tax, and Enterprise Tax.

2. Taxes on Property, etc. :

National Taxes Inheritance Tax, Gift Tax, Land Value Tax, Registration and License Tax, and Stamp Tax.

Local Taxes Automobile Tax, Mine- lot Tax, Property Tax, Light Vehicle Tax, Special Landholding Tax, Business Office Tax, Urban Planning Tax, and Real Property Acquisition Tax.
etc.

3. Taxes on Consumption:

National Taxes Consumption Tax, Liquor Tax, Tobacco Tax, Special Tobacco Tax, Gasoline Tax, Local Road Tax, Liquefied Petroleum Gas Tax, Motor Vehicle Tonnage Tax, Aviation Fuel Tax, Petroleum and Coal Tax, Promotion of Power-resources Development Tax, Customs Duty, Tonnage Due, and Special Tonnage Due.

Local Taxes Local Consumption Tax, Prefectural Tobacco Tax, Golf Course Utilization Tax, Automobile Tax, Municipal Tobacco Tax, Light Vehicle Tax, Bathing Tax, Hunter's Tax, Automobile Acquisition Tax, Light Oil Delivery Tax, and Mineral Products Tax, etc.

Revenue Estimates by Tax Items (FY 2005)

(In 100 million yen)

National Taxes (Budget)			Local Taxes (Estimated)		
Tax item	Amount	%	Tax item	Amount	%
Direct Taxes (Total)	302,354	59.4	1. Prefectural Taxes (Total)	154,308	100.0
Income Tax	127,880	25.1	(1) Ordinary Taxes	138,921	90.0
Corporation Tax	130,580	25.6	Prefectural Inhabitants Tax	35,973	23.3
Inheritance Tax	13,800	2.7	Enterprise Tax	50,593	32.8
Income Tax*(s)	30,094	5.9	Local Consumption Tax	26,343	17.1
			Real Property Acquisition Tax	4,828	3.1
			Prefectural Tobacco Excise Tax	2,848	1.8
Indirect Taxes, etc. (Total)	206,889	40.6	Golf Course Utilization Tax	583	0.4
Consumption Tax	105,380	20.7	Automobile Tax	17,659	11.4
Liquor Tax	15,720	3.1	Mine-lot Tax	4	0.0
Tobacco Tax	9,400	1.8	Prefectural Property Tax	90	0.1
Gasoline Tax	21,560	4.2			
Liquefied Petroleum Gas Tax	140	0.0	(2) Earmarked Taxes***	15,387	10.0
Aviation Fuel Tax	870	0.2			
Petroleum and Coal Tax	4,760	0.9	2. Municipal Taxes (Total)	194,675	100.0
Motor Vehicle Tonnage Tax	7,370	1.4	(1) Ordinary Taxes	179,687	92.3
Customs Duty	9,060	1.8	Municipal Inhabitants Tax	84,333	43.3
Tonnage Due	90	0.0	Property Tax**	84,991	43.7
Consumption Tax*(s)	12,170	2.4	Light Vehicle Tax	1,573	0.8
Local Road Tax* (s)	3,098	0.6	Municipal Tobacco Excise Tax	8,750	4.5
Liquefied Petroleum Gas Tax* (s)	140	0.0	Mineral Product Tax	15	0.0
Aviation Fuel Tax* (s)	158	0.0	Special Landholding Tax	25	0.0
Motor Vehicle Tonnage Tax* (s)	3,685	0.7			
Special Tonnage Due* (s)	113	0.0	(2) Earmarked Taxes****	14,988	7.7
Customs Duty on Oil (s)	5	0.0			
Promotion of Power Resources Development Tax (s)	3,540	0.7			
Gasoline Tax (s)	7,393	1.5			
Special Tobacco Tax (s)	2,237	0.4			
Total	509,243	100.0	Total	348,983	100.0

Note : Taxes marked with (s) are distributed to Special Accounts.

* Distributed to local governments.

** Municipal property tax includes Charges on National Assets and Public Corporations' Assets.

*** Automobile acquisition tax, Light-oil Delivery Tax, etc.

**** Bathing Tax, Business Office Tax, Urban Planning Tax, etc.
(see Appendix VII)

1/3 Tax Laws and Regulations

1. National Taxes

- a. Article 30 of the Japanese Constitution states that “The people shall be liable to taxation as provided by law,” declaring the duty of the people to pay tax. In addition, Article 84 states “No new taxes shall be levied or existing taxes modified except by law or under such conditions as law may prescribe,” laying down the principle that no taxes can be imposed on the people except by law. The principal existing laws are shown in the following table.
- b. In order to implement the provisions of the law, the Cabinet can enact cabinet orders (Paragraph 6, Article 73 of the Japanese Constitution). In addition, each minister can enact ministerial ordinances in order to implement laws and cabinet orders.
- c. The Commissioner of the National Tax Agency issues directives to officials of the National Tax Agency and its local subordinate bureaus, providing a uniform interpretation and application of laws and ordinances. In general, these directives are made public. They are merely the interpretation of the tax authorities, and do not bind judicial courts as a source of law. The final interpretation of laws and ordinances lies with the courts.
- d. Treaties with foreign countries are concluded by the Cabinet but require the approval of the Diet (Paragraph 3, Article 73 of the Japanese Constitution). Treaties are faithfully observed and are given the full force and effect of law. Japan has concluded 45 tax treaties which are applied to 56 countries for the avoidance of double taxation and the prevention of tax evasion concerning taxes on income (see 24/3).

National Tax Laws and Regulations

Classification	Law	Cabinet Order	Ministerial Ordinance
Income Tax	Income Tax Law 31 Mar. 1965 Law No. 33	Cabinet Order Implementing the Income Tax Law 31 Mar. 1965 Cabinet Order No.96	Ministerial Ordinance Implementing the Income Tax Law 31 Mar. 1965 Ministry of Finance Ordinance No.11
Corporation Tax	Corporation Tax Law 31 Mar. 1965 Law No.34	Cabinet Order Implementing the Corporation Tax Law 31 Mar. 1965 Cabinet Order No.97	Ministerial Ordinance Implementing the Corporation Tax Law 31 Mar. 1965 Ministry of Finance Ordinance No.12
Special Corporation Surtax	Special Corporation Surtax Law 31 March 1992 Law No.15	Cabinet Order Implementing the Special Corporation Surtax 31 March 1992 Cabinet Order No.89	Ministerial Ordinance Implementing the Special Corporation Surtax 31 March 1992 Ministry of Finance Ordinance No.15
Inheritance Tax and Gift Tax	Inheritance Tax Law 31 Mar. 1950 Law No.73	Cabinet Order Implementing the Inheritance Tax Law 31 Mar. 1950 Cabinet Order No.71	Ministerial Ordinance Implementing the Inheritance Tax Law 31 Mar. 1950 Ministry of Finance Ordinance No.17
Land Value Tax	Land Value Tax Law 2 May 1991 Law No.69	Cabinet Order Implementing the Land Value Tax Law 21 May 1991 Cabinet Order No.174	Ministerial Ordinance Implementing the Land Value Tax Law 6 June 1991 Ministry of Finance Ordinance No.31
Registration and License Tax	Registration and License Tax Law 12 June 1967 Law No.35	Cabinet Order Implementing the Registration and License Tax Law 26 June 1967 Cabinet Order No.146	Ministerial Ordinance Implementing the Registration and License Tax Law 30 June 1967 Ministry of Finance Ordinance No. 37
Revaluation Tax	Revaluation Tax Law 25 Apr. 1950 Law No.110	Cabinet Order Implementing the Revaluation Tax Law 25 Apr. 1950 Cabinet Order No.95	Ministerial Ordinance Implementing the Revaluation Tax Law 25 Apr. 1950 Ministry of Finance Ordinance No.37
Consumption Tax	Consumption Tax Law 30 Dec. 1988 Law No. 108	Cabinet Order Implementing the Consumption Tax Law 30 Dec. 1988 Cabinet Order No. 360	Ministerial Ordinance Implementing the Consumption Tax Law 30 Dec. 1988 Ministry of Finance Ordinance No.53
Liquor Tax	Liquor Tax Law 28 Feb. 1953 Law No. 6	Cabinet Order Implementing the Liquor Tax Law 31 Mar. 1962 Cabinet Order No.97	Ministerial Ordinance Implementing the Liquor Tax Law 31 Mar. 1962 Ministry of Finance Ordinance No.26

(continued)

National Tax Laws and Regulations (Continued)

Classification	Law	Cabinet Order	Ministerial Ordinance
Tobacco Tax	Tobacco Tax Law 10 Aug. 1984 Law No.72	Cabinet Order Implementing the Tobacco Tax Law 25 Jan. 1985 Cabinet Order No.5	Ministerial Ordinance Implementing the Tobacco Tax Law 25 Jan. 1985 Ministry of Finance Ordinance No.1
Gasoline Tax	Gasoline Tax Law 6 Apr. 1957 Law No.55	Cabinet Order Implementing the Gasoline Tax Law 6 Apr. 1957 Cabinet Order No 57	Ministerial Ordinance Implementing the Gasoline Tax Law 2 Apr. 1962 Ministry of Finance Ordinance No.30
Aviation Fuel Tax	Aviation Fuel Tax Law 31 Mar. 1972 Law No.7	Cabinet Order Implementing the Aviation Fuel Tax Law 31 Mar. 1972 Cabinet Order No.57	
Petroleum and Coal Tax	Petroleum and Coal Tax Law 18 Apr. 1978 Law No.25	Cabinet Order Implementing the Petroleum and Coal Tax Law 18 Apr. 1978 Cabinet Order No.132	Ministerial Ordinance Implementing the Petroleum Tax Law 18 Apr. 1978 Ministry of Finance Ordinance No.25
Motor Vehicle Tonnage Tax	Motor Vehicle Tonnage Tax Law 31 May 1971 Law No.89	Cabinet Order Implementing the Motor Vehicle Tonnage Tax Law 28 Aug. 1971 Cabinet Order No.275	Ministerial Ordinance Implementing the Motor Vehicle Tonnage Tax Law 8 Sept. 1971 Ministry of Finance Ordinance No.66
Local Road Tax	Local Road Tax Law 30 July 1955 Law No.104	Cabinet Order Implementing the Local Road Tax Law 30 July 1955 Cabinet Order No.151	
Liquefied Petroleum Gas Tax	Liquefied Petroleum Gas Tax Law 29 Dec. 1965 Law No.156	Cabinet Order Implementing the Liquefied Petroleum Gas Tax Law 24 Jan. 1966 Cabinet Order No.5	Ministerial Ordinance Implementing the Liquefied Petroleum Gas Tax Law 24 Jan. 1966 Ministry of Finance Ordinance No.4
Stamp Tax	Stamp Tax Law 31 May 1967 Law No.23	Cabinet Order Implementing the Stamp Tax Law 31 May 1967 Cabinet Order No.108	Ministerial Ordinance Implementing the Stamp Tax Law 31 May 1967 Ministry of Finance Ordinance No.19
Tonnage Due	Tonnage Due Law 31 Mar. 1957 Law No.37	Cabinet Order Implementing the Tonnage Due Law 31 Mar. 1957 Cabinet Order No. 48	
Special Tonnage Due	Special Tonnage Due Law 31 Mar. 1957 Law No.38	Cabinet Order Implementing the Special Tonnage Due Law 31 Mar. 1957 Cabinet Order No.49	

(continued)

National Tax Laws and Regulations (Continued)

Classification	Law	Cabinet Order	Ministerial Ordinance
Promotion of Power-resources Development Tax	Promotion of Power-resources Development Tax Law 6 June 1974 Law No.79	Cabinet Order Implementing the Promotion of Power-resources Development Tax Law 27 Sept. 1974 Cabinet Order No.339	
Special Tobacco Tax	Law concerning Special Measures for Financing Debt Transferred to the General Account 10 Oct. 1998 Law No.137	Cabinet Order concerning Special Tobacco Tax 28 Oct. 1998 Cabinet Order No.345	Ministerial Ordinance concerning the Special Tobacco Tax 28 Oct. 1998 Ministry of Finance Order No. 122

In addition to these laws, the following laws are common to all tax laws:

National Tax Laws and Regulations (Continued)

Classification	Law	Cabinet Order	Ministerial Ordinance
General Rules	General National Tax Law 2 Apr.1962 Law No.66 Administrative Appellate Law 15 Sept.1962 Law No.160	Cabinet Order Implementing the General National Tax Law 2 Apr.1962 Cabinet Order No.135	Ministerial Ordinance Implementing the General Law of National Tax 2 Apr.1962 Ministry of Finance Ordinance No.28
Special Taxation Measures	Special Taxation Measures Law 31 Mar.1957 Law No.26	Cabinet Order Implementing the Special Taxation Measures Law 31 Mar.1957 Cabinet Order No.43	Ministerial Ordinance Implementing the Special Taxation Measures Law 31 Mar.1957 Ministry of Finance Ordinance No.15
Exemption, Reduction, or Deferment of Collection of Taxes for Those Who Suffered from Disasters	Law of Exemption, Reduction or Deferment of Collection of Taxes for Those Who Suffered from Disasters 13 Dec.1947 Law No.175	Cabinet Order Implementing the Law of Exemption, Reductions or Deferment of Collection of Taxes for Those Who Suffered from Disasters 13 Dec.1947 Cabinet Order No.268	
National Tax Violation Control	National Tax Violation Control Law 17 Mar.1900 Law No.67	Cabinet Order Implementing the National Tax Violations Control Law 23 Mar.1900 Cabinet Order No.52	
Tax Collection	National Tax Collection Law 20 Apr.1959 Law No.147	Cabinet Order Implementing the National Tax Collection Law 31 Oct.1959 Cabinet Order No.329	Ministerial Ordinance Implementing the National Tax Collection Law 2 Apr.1962 Ministry of Finance Ordinance No.31

Note: The promulgation date and law number are shown immediately following the name of the law in the "Law" column.

The General National Tax Law contains provisions for matters that are common and fundamental to all aspects of taxation, primarily intended to simplify the system for tax laws as well as to clarify the legal basis of taxation. Articles dealing with procedural matters, such as the determination of the tax amount, payment of taxes (see Chapter XIX), postponement of tax payment, pledges for taxes, refunds (see Chapter XXI), and tax disputes (see Chapter XXII) make up the bulk of the Law, but general provisions on additional taxes (see 20/2), on limitation of the period of assessment and collection (see 21/5), and on other areas are also included.

Enactment of the General Law of National Taxes in 1962 laid the ground-work for the simplification and clarification of Japan's tax laws. This Law is designed to make each tax law more understandable.

The Special Taxation Measures Law provides special tax measures directed toward economic policy goals. For example, it provides for special tax rates on interest and for special depreciation. Most of the forms of special tax treatment provided by this Law are temporary.

The Law of Exemption, Reduction, or Deferment of Collection of Taxes for Those Who Suffered from Disasters grants an exemption, reductions or deferment of collection of taxes for victims of a disaster.

The National Tax Violation Control Law stipulates the procedures for investigation and punishment of tax evasion (see 20/3).

The National Tax Collection Law generally stipulates the procedures for the collection of national taxes (see 21/1).

- f. Japan has concluded 45 tax treaties which are applied to 56 countries: Ireland, Azerbaijan the United States, Armenia, the United Kingdom, Israel, Italy, India, Indonesia, Viet Nam, Ukraine, Uzbekistan, Egypt, Australia, Austria, the Netherlands, Canada, Kyrgyz, Georgia, Zambia, Singapore, Switzerland, Sweden, Spain, Sri Lanka, Slovak, Thailand, Czech, Denmark, Tajikistan, Germany, Turkmenistan, Turkey, New Zealand, Norway, Pakistan, Hungary, Bangladesh, Fiji, the Philippines, Finland, Brazil, France, Bulgaria, Belarus, Belgium, Poland, Malaysia, Mexico, Moldova, Romania, Luxembourg, Russia, the Republic of Korea, China, and South Africa.

These conventions include provisions on the method of levying taxes on industrial or commercial profits, exemption from taxes on income derived from the operation of aircraft or ships, reduction of taxes on interest, dividends, and royalties, and tax exemption for temporary visitors.

By international custom, moreover, diplomats are exempted from taxes.

2. Local Taxes

Article 92 of the Japanese Constitution states that “Regulations concerning the organization and operation of local public entities shall be fixed by law in accordance with the principle of local autonomy.” The Local Autonomy Law was enacted on the basis of this provision in the Constitution, and local public entities have been organized and placed in operation. Local public entities consist of *To*, *Do*, *Fu*, *Ken* (prefectures), cities, towns, and villages.

There are 47 prefectures (1 *To*, 1 *Do*, 2 *Fus* and 43 *Kens*) and about 1,800 municipalities (cities, towns, and villages) in Japan (see 23/1).

Article 94 of the Japanese Constitution states that “Local public entities shall have the right to manage their property, affairs, and administration and to enact their own regulations within the law” and Article 223 of the Local Autonomy Law provides that “Local public entities can assess and collect local taxes as provided by law.” Under these provisions, local public entities are given the right to assess and collect local taxes; thus “Local Tax Law” (31 July 1950, Law No. 226) was enacted.

Broadly, the Local Tax Law consists of 4 chapters; (1) General Rules, (2) Ordinary Taxes for *To*, *Do*, *Fu*, and *Ken* (prefectures), (3) Ordinary Taxes for Cities, Towns, and Villages, and (4) Earmarked Taxes (see Chapter XXIII).

Unlike national tax laws, the Local Tax Law does not directly mandate that residents pay taxes. It only confirms the right of local public entities to assess and collect taxes within a framework prescribed by law. The regulations enacted by each local public entity mandate that residents pay local taxes.

CHAPTER II

INCOME TAX (INDIVIDUAL INCOME TAX)

2/1 General

1. Characteristics of Japan's Income Tax

- a.** The individual income tax and the corporation tax (corporate income tax) are treated separately under the Income Tax Law and the Corporation Tax Law, respectively.
- b.** Taxable individual income, unlike corporate income, is computed on a calendar year basis, from 1 January through 31 December; individuals have no choice as to the length of the accounting period.
- c.** Under the Income Tax Law, taxable income is classified for the purpose of calculation into the following ten categories in accordance with the nature of the income, taking into consideration the capacity for taxation as well as the convenience of calculation.

- | | |
|------------------------|---------------------------|
| (1) Interest income | (6) Retirement income |
| (2) Dividend income | (7) Timber income |
| (3) Real estate income | (8) Capital gains |
| (4) Business income | (9) Occasional income |
| (5) Employment income | (10) Miscellaneous income |

- d.** Income tax is to be assessed primarily on the basis of an individual's aggregate income, regardless of its category. Individual taxpayers must pay income tax on the total income earned during the calendar year concerned.

Retirement income and timber income, however, are taxed separately from the other categories of income under the Income Tax Law. Interest income is taxed separately from the other categories of income under the Special Taxation Measures Law. Dividend income and capital gains etc. are, or may be, taxed separately as well (for details, see **2/3, 9**).

- e.** Income tax rates are progressive, ranging from 10% to 37% (5% to 40% from 2007) (see **2/5, 1**). However, interest income mentioned in item "d" above is taxed separately at the source at special rates specified in the Special Taxation Measures Law, and dividend income may be so taxed as well (see **2/3, 9**). In addition, specific capital gains etc. are taxed at special rates provided for under the same Law (see **2/3, 6**).
- f.** For the determination and payment of taxes due, income tax is assessed under the self-assessment system, under which income tax liability is determined by the taxpayer's declaration based on proper records of the tax base

and the tax amount due, and payment is made on this basis. In the event a taxpayer fails to file a correct return, the tax authority makes an assessment through examination and conducts “correction” or “determination”. Almost all wage and salary earners, however, are not required to file final returns, owing to the withholding system and year-end adjustment system (see 2/1, g. and 2/8, 4).

g. A withholding system is frequently used. For the convenience of tax collection, a withholding mechanism requires the payer of the following categories of incomes to compute the amount of income tax, deduct that amount at the time of payment, and transmit it to the government.

- (1) Interest income
- (2) Dividend income
- (3) Profit from redemption of discount bonds
- (4) Employment income
- (5) Retirement income
- (6) Miscellaneous income from public annuities etc.
- (7) Fees or other remunerations* for certain services, such as writing or speeches, and the services of lawyers, movie actors, professional baseball players, etc.
- (8) Income from business that provides the personal services of artists and public entertainers.
- (9) Contract deposits received by professional baseball players, etc. for services to be rendered, prizes for advertising purposes, and prizes received by owners of racehorses.
- (10) Annuity from life insurance contract
- (11) Quasi-financial products
- (12) Distribution of profits from anonymous associations

2/2 Taxpayers

1. Taxpayers and Taxable Income

Taxpayers with respect to income tax are divided into resident taxpayers and nonresident taxpayers.

a. Resident Taxpayer

An individual who has a “Jusho” (domicile),** or has had a residence for one

* Withholding is not applicable when such fees or other remunerations are paid by individuals who are not required to withhold income tax on payment of employment income.

** An official of the national or local government of Japan who resides abroad is deemed to have a “Jusho” in Japan for the period when he does not have a domestic “Jusho”.

year or more in Japan (here after referred to as a “resident”) must pay income tax on all of his or her income from both within and outside Japan. A resident who doesn’t have the Japanese nationality and who has had domicile or residence in Japan for no more than five years in the past ten years (non-permanent resident), however, is subject to tax only on the total income derived from sources within Japan and on the income from other sources paid in Japan or remitted to Japan from abroad.

b. Nonresident Taxpayer

An individual who has no Jusho and has had residence in Japan for less than one year (here after referred to as “nonresident”) must pay income tax on his income from sources within Japan (for details, see 24/1).

c. Corporation*

In principle, income tax is imposed only on individuals, but corporations are to pay income tax at source as follows. However, corporations under the category of nontaxable corporations specified by the Income Tax Law (such as government agencies, local authorities, and corporations fully owned by the government or established in the public interest) are not to pay income tax for on the following incomes:

- (1) Corporations which have their head office in Japan: interest, profit from redemption of discount bonds dividends, quasi-financial products, Distribution of profits from anonymous associations, or prizes received by owners of race-horses paid in Japan.
- (2) Corporations which do not have their head office in Japan: distribution of the profit from the business of associations, gains from the transfer of the land, the rent of immovable property, interest, dividends, remuneration for personal services, royalties for industrial property rights or copyrights, interest on loans, or rent or other income derived from sources within Japan (see 24/2).

* For the purposes of the Income Tax Law, the term “corporation” includes (1) juridical persons established under the Corporate Code, the Civil Code, or any other law, for instance, joint stock companies, Japanese version LLC (Godo-Kaisha) and other companies, cooperative associations, or foundations, and (2) non-juridical organizations which have a designated representative or manager.

2. Rules for Income Attribution

a. Principle of Attribution of Income to an Actual Beneficiary^{*}

- (1) Income is attributed, in principle, to the actual beneficiary of economic gain and not to the person acting merely as an intermediary such as an agent or nominee. For example, if a stock is held in the name of A, but B actually enjoys its dividends, the income tax on such dividends is imposed not on A but on B.
- (2) Take, for example, a corporation which has 15 or more business places, if in two-thirds or more of the business places the directors (including the relatives of such directors) who formerly carried on the same business as individual taxpayers in the same places are still in charge of business carried on there, the individual income tax is imposed on the presumption that such directors actually receive the gains accruing from those business places. The purpose of this measure is to prevent proprietors from reducing their tax burden by organizing an association in corporate form and paying the corporation tax although each of them is still in fact carrying on business as a proprietor.

b. Attribution of Profits from Trust Property

Profits with relation to trust property are attributed to the following persons:

- (1) If the beneficiary of a trust is specified; the beneficiary.
- (2) When the beneficiary is not specified or does not exist; the settlor. Excluding a joint operation trust^{**} or a securities investment trust^{***}.

^{*} The principle of attribution of income to an actual beneficiary is applicable not only to the determination of taxpayers, i.e., to the determination as to whom certain income is attributable, but also to the determination of the tax base. For example, in the case where an act or transaction of a family corporation is considered to result in an unfair reduction of the income tax burden on the shareholder (including a relative or employee in a special relationship with said shareholder), the tax authorities may, disregarding the act or transaction in question, compute at their discretion the amount of income tax due. For instance, if a family corporation sells a house which it owns to its president at a price substantially lower than the market price, the corporation is not allowed to compute its income on the basis of such a transaction. In other words, the amount equal to the price difference is regarded as income for the corporation and is taxable under the Corporation Tax Law. In addition, income tax is imposed on the amount because the amount is also regarded as constituting a bonus received by the president. Income derived from illegal sources is also taxable so long as the economic gains there from are attributable to the taxpayer.

^{**} A “joint operation trust” is a monetary trust under which a trust company manages funds entrusted by many separate and independent settlors. A loan trust under the Loan Trust Law falls into this category.

^{***} A “securities investment trust” is a trust fund operated by an entity having legal title thereto, while the beneficial interest is held by those purchasing interests therein, such interests being represented by trust certificates. The Investment Trust Law and the Investment Corporation Law provides the basis for establishment and operation of these trusts.

2/3 Calculation of the Tax Base

1. Principles of Taxable Income Calculation

- a. Taxable income is calculated in principle by deducting necessary expenses from gross receipts. As will be mentioned later, however, there are some exceptions or modifications to this principle (see 2/3, 2). For example, the amount of interest income is equal to the gross receipts. In the case of employment income, a certain percentage of receipts (prescribed by the Income Tax Law) is deducted from total receipts. In the case of timber income, a taxpayer can choose whether to deduct actual costs or to deduct estimated costs instead of actual costs.
- b. The amount of receipts is determined in principle when the amount to be received is determined (accrual basis). However, as to interest on bearer bonds the amount of receipts is determined when such interest is actually received.
Small business proprietors who file a blue return (see 2/7) may compute their income on a cash basis.
- c. The amount of receipts includes not only money received but also the value of other properties or economic benefits received. In such a case, value is determined at the time of the receipt of such properties or economic benefits. The economic benefit, for this purpose, does not include so-called “imputed income.”
- d. The appraisal gain of assets is not treated as taxable income, and therefore the appraisal loss of assets is not deductible from taxable income.
- e. “Expenses” mean, as a rule, the necessary expenses needed directly for acquiring income and those incurred during the taxable year for the conduct of business to obtain the income, such as selling expenses and executive and general administrative expenses. Generally speaking, expenses not directly connected with the acquisition of income, such as contributions to schools, interest paid on personal debts, and ordinary losses incurred on non-business properties, are not deductible as necessary expenses. Expenses relating to housekeeping, like a taxpayer’s living expenses, income tax, and inhabitants tax are not deductible as necessary expenses.
- f. The taxable year for individuals begins on 1 January and ends on 31 December. When a taxpayer dies or ceases business in the course of a year, the taxable year ends at that time. When a taxpayer starts business in the course of a year, the taxable year begins at that time.
- g. The basic principle for calculating the taxable income is to deduct necessary expenses from receipts. However, if the taxpayer does not keep accounting

Income Tax (Individual Income Tax)

books properly, the tax authorities are empowered to assess his or her income by estimation, on the basis of an increase or decrease in assets and liabilities, receipts and expenses, and the size of the business.

2. Categories of Income and Method of Calculation

Categories of Income	Scope	Method of calculation
(1) Interest income	Interest on deposits, bonds and the distribution of gains of a joint operation trust and bond investment trust. Excluding the refund of principal from the distribution of gains of open-end securities investment trusts or special purpose trust. Income tax is not assessed for such income as mentioned in 2/3, 8(1)~(7).	Interest receivable in the year (as for interest on bearer bonds or distributions of gains on beneficiary certificates of unscribed loan trusts and bond investment trusts, the amount of money actually received). Interest income is taxed separately from other income (see 2/3,9).
(2) Dividend income	Distribution of surpluses from a corporation, dividends of profits, interest during construction, or distribution of gains of an investment trust (excluding bond investment trusts).	Gross dividends receivable in the year (as for dividends on shares of bearer stock or distributions of gains on beneficiary certificates of unscribed securities investment trusts, or special purpose trust the amount of money actually received) less the interest in indebtedness incurred for the acquisition of the principal. A taxpayer can have an option not to file a return on certain dividends. (see 2/3,9).
(3) Real estate income	Income from the lease of real estate, rights on real estate, or ships or aircraft (excluding income falling into categories of business income and capital gains).	Gross receipts less the necessary expenses for the year.
(4) Business income	Income derived from business activities such as commerce, manufacture, mining, agriculture, fishery, medical service, authorship or other continuous businesses except for timber income and capital gains.	Gross receipts less the necessary expenses for the year. For agriculture, gross receipts from farm products are generally calculated on the basis of the price at the harvest time.

(continued)

2. Categories of Income and Method of Calculation (Continued)

Categories of Income	Scope	Method of calculation
(5) Employment income	Salaries, etc., including wages, bonuses, and other allowances of a similar nature. Income tax is not assessed for such income as mentioned in 2/3,8 (9)~(14), e.g., a reasonable amount for the commuter allowance. Amount of contributions based on the public pension system etc. (for investment in life insurance, mutual-aid life insurance, trusts, or securities investment trusts) disbursed by an employer for his employees' sake is not treated as employment income salaries, etc.	The amount of salaries, etc., in the year less the following amounts (employment income deduction): (a) If salaries do not exceed ¥1,800,000, the deduction is 40% of salaries, etc., but the minimum guaranteed amount is ¥650,000. (b) If income receivable exceeds ¥1,800,000 yen but not ¥3,600,000, the deduction is ¥180,000 plus 30% of salaries, etc.. (c) If income receivable exceeds ¥3,600,000 but not ¥6,600,000, the deduction is ¥540,000 plus 20% of salaries, etc.. (d) If income receivable exceeds ¥6,600,000 but not ¥10,000,000, the deduction is ¥1,200,000 plus 10% of salaries, etc.. (e) If income receivable exceeds ¥10,000,000, the deduction is ¥1,700,000 plus 5% of salaries, etc., Deduction for specific expenses is allowed in certain conditions (see 2/3, 4).
(6) Retirement income	Lump sum pensions, retirement allowances, and other allowances of a similar nature. Lump sum retirement allowances paid by the social insurance system, qualified pensions*, and lump sum payments based on contracts are considered to be retirement benefit.	50% of retirement income during the year after the special retirement deduction. The amount of deduction is calculated as follows: (a) If the period of service is 20 years or less, the deduction is working years × ¥400,000, but the minimum guaranteed amount is ¥800,000. (b) If the period of service is more than 20 years, the deduction is ¥8,000,000 plus (working years - 20 years) × ¥700,000. Retirement income is taxed separately from other income.

(continued)

* “Qualified pensions” are pensions paid to employees upon retirement by the insurance company or trust company which is engaged in the business of retirement pensions. The corporation (employer) makes a contract with and pays contributions to these companies. When such contributions are made, tax is not imposed on pensioners (employees). Thus, taxation is deferred until the time of retirement.

“Qualified pensions” will be abolished after implementing a certain transitional measure (a measure to transfer to defined benefit corporate pensions, etc., until March 31, 2012).

2. Categories of Income and Method of Calculation (Continued)

Categories of Income	Scope	Method of calculation
(7) Timber income	Income derived from the lumber or transfer of timber (excluding income derived from the sale or transfer of timber within a short period of time from the date of acquisition).	Gross receipts, less expenses for forestation, acquisition, management, and lumbering of the forest, other necessary expenses and a special deduction of ¥500,000. Timber income is taxed separately from other income. (special case, see 2/3,5)
(8) Capital gains	Income derived from the transfer of assets (including income from lump sum payments for the lease of land or right to use land, but not including timber income and income from transfers of inventories and regular pro fit making transfers of assets).	<p>(1) The principal method of computation is as follows:</p> <ul style="list-style-type: none"> (a) First, divide total capital gains into two categories, short-term capital gains and long-term capital gains. (b) Deduct costs of acquisition and expenses for installation, improvement and disposal of assets from the gross receipts of the two types of capital gains, respectively. (c) Add the two types of net capital gains calculated in (b) above. (d) Subtract ¥500,000 as the special deduction from the total calculated in (c) above. <p>The special deduction must first be applied to the net short-term capital gains. The remaining amount is deducted from to the net long-term capital gains.</p> <ul style="list-style-type: none"> (e) Then, net taxable capital gains are as calculated below: the net short-term capital gains after the special deduction plus 50% of the sum of net long-term capital gains after the special deduction. <p>(2) Capital gains from sale or transfer of land or buildings, however, are taxed separately from other income under the Special Taxation Measures Law (see 2/3,6d-k).</p> <p>Capital gains from sale of securities are taxed separately from other income under the Special Taxation Measures Law (see 2/3,6l).</p>

(continued)

2. Categories of Income and Method of Calculation (Continued)

Categories of Income	Scope	Method of calculation
(9) Occasional income	<p>Income of an occasional nature (excluding those items similar in nature to remuneration for personal services and to income derived from the alienation of properties) other than those items enumerated in (1) to (8) above, which is not derived from regular pro fit making activities.</p> <p>Occasional income includes winnings gained from horse-races and prizes in any contest, such as television and radio quiz programs.</p> <p>It also includes proceeds derived by an employee from investment in life insurance, mutual-aid life insurance, trusts, or securities investment trusts made by an employer for an employee's sake under the Employees' Assets Formation System.</p> <p>Income tax is not assessed for such income as mentioned in 2/3,8(8)(9).</p>	50% of net income after deducting the amount of expenses used to obtain this income, and subtracting ¥500,000 as a special deduction.
(10) Miscellaneous income	<p>(a) Income other than that enumerated in the preceding items (including commissions for manuscripts earned by a nonprofessional writer and interest other than that enumerated in (1) interest income or (4) business income) and</p> <p>(b) Public annuity income, etc. (including pensions and annuities paid by the social insurance system and qualified pensions).</p>	<p>(A) Gross receipts subtracting necessary expenses,</p> <p>(B) The amount of public annuities, etc. in the year subtracting less the following amounts of public annuities deduction: (the minimum guaranteed amount is ¥700,000 (¥1,200,000 for a taxpayer over 65 years of age))</p> <p>(a) First subtract ¥500,000 as the fixed amount deduction.</p> <p>(b) If the amount of public annuities, etc., after the fixed amount deduction does not exceed ¥3,600,000, the deduction is 25% of that amount.</p> <p>(c) If the amount of public annuities, etc., after the fixed amount deduction exceeds ¥3,600,000 but not ¥7,200,000, the deduction is ¥360,000 plus 15% of that amount.</p> <p>(d) If the amount of public annuities, etc., after the fixed amount deduction exceeds ¥7,200,000, the deduction is ¥1,080,000 plus 5% of that amount.</p>

3. Calculation of Business Income

The amount of business income is calculated by deducting necessary expenses from gross receipts.

a. Calculation of Gross Receipts

- (1) Gross receipts of a business are the total of receipts in connection with business activities calculated on an accrual basis. Certain small business proprietors who file a blue return may calculate their income on a cash basis.
- (2) The total of receipts from farm products is generally calculated on the basis of the price at harvest time.

b. Calculation of Necessary Expenses

- (1) Necessary expenses in general

Necessary expenses deductible in the calculation of business income are those directly necessary to acquire the receipts and those arising from the conduct of business to obtain the business income during the year. The main items of necessary expenses are: cost of merchandise sold; depreciation allowance for fixed assets; depreciation allowance for deferred assets; repairs for buildings or other properties used for business; rental fees for buildings or land used for business; insurance premiums for buildings or other properties used for business; taxes and levies on buildings, land, or other properties used for business; wages for employees; interest on business indebtedness and; bad debts. Expenses relating to housekeeping, income tax, and local inhabitants tax are not counted in necessary expenses. Bribes paid to domestic and foreign public officials cannot be included in expenses in income tax calculations. Article 37 of the Income Tax Law provides that deductible items are expenses directly necessary for gaining revenue, but illegal expenditures such as bribes cannot be considered as expenses directly necessary for gaining revenue.

- (2) Special treatment of fees for medical care under the social insurance system

In the calculation of income derived by physicians and dentists from fees for medical care under the social insurance system, a graduated lump sum deduction of 57%, 62%, 70%, and 72% calculated on portions of gross receipts of such fees may be selected in lieu of actual necessary expenses. If the amount of these fees exceeds ¥50,000,000, this special treatment is not applicable.

- (3) Deduction for family employees

In principle, salaries or wages paid to employees are deductible as necessary expenses in computing taxable income from business. Salaries or wages paid to relatives who live together with the taxpayer (family employees), however, are deductible only in certain conditions. The deduction is deemed as salaries or wages in the following amounts only when the family employee is engaged solely in the business of the taxpayer and is more than 15 years old:

- (a) If a taxpayer files a blue return as well as a notice of his family employees, the amount paid to the family employee as reported in the notice can be deducted as necessary expenses within the range of the reported amount, if these are considered reasonable compared to ones paid to employees in other enterprises of the same type and in the same scale.
- (b) If a taxpayer does not file a blue return, a deduction of ¥860,000 is allowed for his or her spouse as a family employee and a deduction of ¥500,000 per person is allowed for other family employees. These are a fixed amounts, whether actually paid or not.

These amounts, ¥860,000 and ¥500,000, shall be treated as the employment income to a family employee, and shall be added to the employment income of the family employee to determine the taxable income of the family employee.

Treatment for the purpose of salaries or wages paid to family employees has been one of the most controversial issues in Japan. In computing business income (real estate income and timber income), the deduction of salaries for family employees is a major problem because most proprietors of family business (e.g., farming) actually do not pay salaries or wages as such to family employees living with them. Furthermore, such proprietors customarily have the right to dispose of the earnings from common family undertakings. To allow in full as necessary expenses the nominally claimed salaries of family employees is neither realistic nor reasonable in terms of equity.

Some proprietors of small-and-medium-sized enterprises, however, actually pay salaries to family employees. Taking this fact into account and for the purpose of keeping in balance the tax burdens upon enterprises run by individual proprietors and those in corporate form, salaries and wages paid to family employees were made deductible as expenses up to a certain limit for taxpayers filing blue returns in the revision of 1952. The change was based on the stipulation that taxpayers filing blue returns were required to keep proper books and records and would be able, therefore, to calculate their business income separately from their household expenses. Needless to say, this measure was intended to en-

courage more taxpayers to file a blue return.

Since 1952, there has been a persistent demand for more liberal exemptions for salaries or wages to eliminate the discrimination against individual proprietors relative to family corporations. Accordingly, the limit set on the deduction for salaries and the like to family employees had increased commensurate with the increase in the basic exemption or deduction for dependents. In 1968, this legal limit was eliminated.

Taxpayers who are not approved to file a blue return (here after referred to as “taxpayers filing a white return”) sought the deduction of family employees’ salaries to a certain extent in order to mitigate their tax burden. The revision of 1961 introduced a deduction for family employees’ salaries for taxpayers filing a white return.

(4) Reserve for bad debts

(a) Reserve for bad debts concerning debentures individually evaluated

If a taxpayer runs a business by which real estate income, business incomes or timber income is earned, the amount carried over to reserve for bad debts as an estimated amount of loss from bad debts such as accounts receivable, loans, and advanced monies, etc., up to a constant amount assumed to be the total amount of the loss concerning the loans, etc., on 31 December (a limited amount of carrying over) is counted as a necessary expense in the calculation of income for the year.

(b) Reserve for bad debts concerning debentures collectively evaluated

If a taxpayer runs a business by which business income is earned and files a blue return, the amount carried over to reserve for bad debts as an estimated amount of loss from bad debts such as accounts receivable, loans, and advanced monies, etc. (excluding the amount that was the basis for the calculation of the “limited amount of carrying over” mentioned in (a)), up to 5.5% (3.3% for those who engage in the banking business) of the total book value of loans such as accounts receivable, etc. on 31 December is counted as a necessary expense in the calculation of income for the year.

(c) The amount counted as a necessary expense in (a) and (b) should be added back to the gross receipts in the following year.

(5) Reserve for loss on returned goods

If a taxpayer who files a blue return and is engaged in the publication or wholesaling of books and magazines, or the manufacturing or wholesaling of pharmaceuticals, agricultural chemicals, cosmetics, ready-made suits, or phonograph records makes the major part of his inventories for sales under repurchasing contracts, an allowance for loss on returned unsold goods is deductible as an estimated amount of loss from repurchasing. This allowance

is computed on the basis of the ratio of returned goods unsold to total sales in the current and previous years. The amount deducted must be added back to the income in the following year.

(6) Reserve for retirement allowances

Provisions to reserve for retirement benefits, made by blue-return tax-payers who engage in business that generates business income, to apply to retirement benefits are included in necessary expenses in calculating the total amount of business income for the fiscal year when the provisions are made.

(7) Other treatments granted only to taxpayers who file blue return are: (i) special income tax credit for incremental research and development expenses (special income tax credit for research and development starting in 2007), (ii) special depreciation of specific equipment, (iii) additional depreciation of specific medical-use buildings, (iv) reserve for the prevention of mineral pollution of metal mining, (v) special deduction for prospecting for new mineral deposits, (vi) application of shorter useful lives of assets or increase of depreciation allowances for machinery being used more intensively than is normal or under adverse conditions, etc.

(8) The amount of premium paid by an employer for the employees' sake under the defined benefit system of business annuity or defined contribution annuity system, etc. are deductible as a necessary expense of the employer.

c. Special Deduction for Filing a Blue Return

Taxpayers filing blue returns are entitled to a special deduction. The deduction is applied to three categories of income in the order of 1) real estate income, 2) business income, and 3) timber income.

The deduction is applicable to individuals filing blue returns:

- (1) Those gaining business income or real estate income and keeping accounting records in accordance with the principle of orderly bookkeeping
.....deduction of ¥650,000
- (2) Other individuals
.....deduction of ¥100,000

d. Separate Taxation of Business Income and the like regarding Land and other Holdings of Real Estate Dealers and the like.

Incomes realized by the transfer of land etc. owned consecutively for 5 years or less as of 1 January of the year in which the sale took place and categorized either as business income or miscellaneous income (commissions falling under these categories of income as being virtual capital gains are also included) are taxed separately from other income. The amount of income tax is

Income Tax (Individual Income Tax)

calculated by comparing 40 percent of the business income from land etc. and 110 percent of the amount of income tax related to business income from land etc., which is derived by applying principal global taxation. Either of which is larger than the other is determined to the amount of income tax. This measure does not apply to sales to the state and to local public entities. However, this measure is suspended from 1998 to 2008.

4. Special Tax Treatment of Employment Income Deduction for employees' specific expenses

If the amount of specific expenses in the year exceeds the amount of deduction for employment income mentioned in 2/3,2(5) above, it is deductible in addition to the deduction for employment income. Specific expenses are :

- (a) certain expenses for commuting;
- (b) certain expenses for transfer;
- (c) certain expenses for training necessary for business;
- (d) certain expenses for obtaining qualifications and;
- (e) certain expenses of going back to home for an employee working apart from his or her family.

Each item needs to be certified by the payer of the salary or the like.

5. Special Tax Treatment of Timber Income

a. Estimated Deduction from Timber Income

When an individual deforests or transfers timber owned for 15 years or longer, the amount of necessary expenses in computing timber income may be obtained by multiplying the amount of gross receipts from such deforestation or transfer by 50%.

b. Special Deduction for Timber Income from Forest Programs

In case an individual has deforested or transferred timber in accordance with certain forest programs during the period of 1 January 1981 through 31 December 2007, the taxpayer may deduct as a special deduction for forest programs 20% of gross receipts from timber income in arriving at the timber income.* However, the deforestation or transfer of timber for the construction of resort institutions is excluded.

* In cases where the authorization for a forest programme is cancelled, this special deduction is not allowed.

6. Special Tax Treatment of Capital Gains

Certain categories of capital gains are given special tax treatment as described below based on the tax-paying ability of the taxpayers concerned.

a. Acquisition Cost

The acquisition cost of property acquired before 1953 is recognized to be equal to the value of the property appraised as of 1 January 1953 for the purpose of computing capital gains. The appraised value of the property as of 1 January 1953 is determined according to the standards published by the National Tax Administration in 1953. However, an amount equal to 5% of the selling price of land, buildings, or right to use land acquired before 1953 is deemed to be the acquisition cost of such property, unless actual costs prove to be more than the amount so determined.

b. Recognition of Capital Gains Based on Market Value

The transfer of assets through giving as a gift, inheritance, bequest, or sale at a notably low price (half of the current price) does not result in capital gains, in principle, since the transferee inherits the cost basis and the time of acquisition of the assets. However, in the cases described below, he or she is deemed to have received such assets at the market price and therefore the transferor is subject to taxation on the capital gains:

- (1) gift or sale to a corporation at a notably low price;
- (2) inheritance, when successors accept heritage on the condition that they are liable for the inherited debts within the limit of the inherited assets and;
- (3) bequest to a corporation and general bequest** to individuals which is accepted on the condition that they are liable for the taxpayer's debt within the limit of the bequeathed assets.

c. Exchange of Land, Buildings, etc.

When land, buildings, ships, or machinery and equipment owned by a taxpayer for one year or longer are exchanged for other properties of the same kind which were owned by other persons for one year or longer and which were acquired not for the purpose of the exchange and, further, the newly acquired property is used in the same way, such property is treated as not being transferred, and the cost basis of the property exchanged is treated as that of newly acquired property.

** A form of bequest which specifies only a ratio of assets to be bequeathed to the total estate.

【Special Tax Treatment of Capital Gains from the Transfer of Land, Building or Right to Use Land (d. - k.)】

d. Special Tax Treatment of Capital Gains Derived from Transfer of Land, Buildings, or Right to Use Land: Principle

Capital gains derived from the sale or transfer of land, buildings, or right to use land are taxed separately from other income.

The tax rates applicable to such capital gains are as follows:

(1) Long-term Capital Gains

Capital gains from continuous ownership for over 5 years as of 1 January of the year in which the transfer was made.

(a) general provision

15% of T.L.C.G. (Taxable long-term capital gains)

(b) In the case of transfer of land or right to use land to the state, local public entities or other specified public entities or to individuals or corporations preparing large-scale and desirable housing sites, T.L.C.G. is taxed as follows:

a. In case where T.L.C.G. is ¥20 million or less:

10% of T.L.C.G.

b. In case where T.L.C.G. exceeds ¥20 million:

$¥2 \text{ million} + 15\% \times (\text{T.L.C.G.} - ¥20 \text{ million})$

(c) Capital gains from residential property continuously owned for over 10 years as of 1 January of the year in which the sale was made (long-term capital gains)

The amount of capital gains is taxed as follows:

a. T.L.C.G. of ¥60 million or less;

10% of T.L.C.G.

b. T.L.C.G. over ¥60 million;

$¥6 \text{ million} + 15\% \times (\text{T.L.C.G.} - ¥60 \text{ million})$

(2) Short-term Capital Gains

Capital gains from property owned for not more than 5 years as of 1 January of the year in which the transfer was made.

30% of taxable short-term capital gains

e. Special Tax Treatment of Capital Gains Derived from Expropriated Property etc.

(1) Ordinary concessions for acquisition of replacement property

(a) If a taxpayer has been expropriated from his or her land or other property, including the right to use the land, under the Land Expropriation Law, the City Planning Law, the River Law, and other laws spends all

the proceeds from expropriation for acquiring replacement property, or if such a taxpayer acquires, from the expropriator, property of the same type as the expropriated property in lieu of the payment for expropriation, such a transaction is treated as non-existent for tax purposes.

- (b) If a taxpayer spends part of the proceeds from expropriation to acquire replacement property, only the amount of such proceeds exceeding the cost of the replacement property is taxable.

In such cases, however, the special deduction of ¥50 million mentioned below is not applicable.

- (2) Special deduction of ¥50 million

If a taxpayer acquires replacement property as a result of expropriation but does not receive the treatment mentioned in (1) above, or if he or she acquires no replacement property, a special deduction of ¥50 million is applicable on the condition that he or she surrenders this property within six months of the offer under expropriation.

f. Special Tax Treatment of Capital Gains for Specific Public Projects

- (1) Special Land Rearrangement Capital Gains Deduction

A taxpayer is entitled to a special deduction of ¥20 million from such capital gains in the following cases:

- (i) a taxpayer transfers his or her land or right to use the land to the state, local public entities, or Urban Renaissance Agency or other public corporations engaged in the supply or development of land for the purpose of improving public facilities or housing land development under special projects such as land rearrangement projects.
- (ii) a taxpayer transfers to local public entities and other entities his or her land or right to use the land, under such special laws as the Law for Preservation of Ancient Cities etc.

- (2) Special Deduction from Capital Gains for Specific Housing Land Development Projects, etc.

A taxpayer is entitled to a special deduction of ¥15 million from such capital gains in the following cases:

- (i) a taxpayer transfers his or her land, including the right to use the land for projects carried out by public entities in charge of the supply or development of residential land or housing or of improvement of the residential, business, agricultural, or transportation environment, etc.
- (ii) a taxpayer transfers his or her land, including the right to use the land to local public entities on the basis of special laws such as the Law Concerning Promotion of Expanding Publicly Owned Land, etc., which are enacted promote the effective use of land from various public viewpoints,

etc.

(3) Special Capital Gains Deduction from the Rationalization of Farmland

If a taxpayer transfers his or her land, including the right to use the land, for the purpose of rationalization of farm land ownership, he or she is entitled to a special deduction of ¥8 million from such capital gains.

g. Special Tax Treatment for Capital Gains on Residential Property

(1) Special Capital Gains Deduction on Residential Property

If a taxpayer transfers his or her house or the house with the land (including the right to use the land) in which they are actually resident he or she is entitled to a special deduction of ¥30 million.

This special deduction may also be applied to transfers that take place within the year the taxpayer ceased to inhabit the house or in the three years that follow.

(2) Special Tax Treatment of Replacement of Residential Property Acquired by Inheritance or Bequest

If a taxpayer who has transferred residential property acquired by inheritance or bequest from father/mother or grandfather/grandmother a house and its land (including the right to use it) upon which the residence has been located for more than 30 years – continuously owned for over 10 years as of 1 January of the year in which the sale was made, acquires other residential property during the specific period (in principle, the year when such transfer took place or the year preceding that year) and puts it to use as his or her own residence by the end of the year following acquisition, the following special measures are applicable:

(i) If the transfer price of the property does not exceed the acquisition price of the newly acquired property, transfer of that property is disregarded, and the capital gains from that transfer are not taxable and;

(ii) If the transfer price of the property exceeds the acquisition price of the newly acquired property, transfer of that property is deemed to have taken place only to the parts in which the transfer price exceeds the acquisition price of the newly acquired property, and the capital gains subject to tax is calculated as the difference between the transfer price and the acquisition price of the newly acquired property.

These special measures also apply to the exchange of residential property where such conditions are satisfied.

(3) Special Tax Treatment for the Replacement of Certain Residential Property

If a taxpayer who has transferred residential property between 1 April 1993 and 31 December 2006 – his or her house and the land (including the

right to use it) – continuously owned for over 10 years as of 1 January of the year in which the sale takes place, acquires another residential property during the specific period (in principle, the year when the sale takes place, or the year preceding that year) and puts it to use as his or her own residence by the end of the year following acquisition, the special measures (as detailed in sections f (2) (i) and (ii), above) are applicable under the following conditions:

- (i) The transferred property should continuously be used as a residence for more than 10 years and;
- (ii) The floor space of the acquired house should be more than 50 m² and less than 280 m², and the area of the acquired land should be less than 500 m².

h. Special Tax Treatment for the Replacement of Business Asset

If an individual taxpayer who has replaced his or her land or buildings, etc., held for business use, and located in a specified area during the period from 1 January 1970 to 31 December 2011 (a part of treatment is effective by 31 December 2006), acquires the land, including buildings thereon, located in another specified area during the specified period (in principle, in the year when the transfer took place or the preceding year), and puts it into business use within a year after acquisition, the following special measures apply:

- (i) If the transfer price of the property (land, buildings, etc.) does not exceed the cost of the newly acquired property, transfer of that property is deemed not to have taken place, and 20% of the capital gains from such a transfer are taxable and;
- (ii) If the transfer price of the property exceeds the cost of the newly acquired property, a transfer of that property is deemed to have taken place only to the parts in which the sale price exceeds 80% of the cost of the newly acquired property, and the capital gains representing the difference between the sale price and such cost are subject to tax.

These special measures are also applicable to the exchange of property held for business use, if such conditions are satisfied.

These special measures are not applicable to replacement of land etc, that is not owned for more than five years (excluding the transfer of land etc. between January 1 2008 to December 31 2008).

These special measures are applicable only if the relocation is generally consistent with national land policy. Seventeen types of displacement are recognized.

i. Special Tax Treatment for Replacement of Lands used for the Construction of Mid-rise and High-rise Fireproof Buildings

In order to utilize already cramped areas more effectively through construction of buildings, special tax treatment in the form of deferral of the tax on capital gains is available to ① those who sell their lands and buildings in Tokyo, Osaka, Nagoya, their suburbs, districts subject to the Redevelopment District Plan and areas under the Central City Invigoration Law and acquire in whole or in part fireproof condominiums with three or more stories and to ② those who sell their lands and buildings in Tokyo, Osaka, Nagoya and certain other large cities (including their suburbs) and acquire in whole or in part fireproof commercial buildings with four or more stories.

j. Special Tax Treatment for the Acquisition of Land through an Exchange Arranged by the Agriculture and Residence Association

If a member of the Agriculture and Residence Association (No-ju Kumiai) acquires land through the exchange of his or her land under the Agriculture and Residence Law, the value of the acquired land and the transferred land are considered to be equal.

k. Special Tax Treatment for Exchange of Land in Large-scale Housing and Land Development Projects

If a taxpayer exchanges land located in an area where a large-scale housing land development project is held for residential plots developed in the same area, he or she is entitled to a deferral of the tax on capital gains.

l. Special Tax Treatment of Capital Gains Derived from the Transfer of Securities

Capital gains derived from the transfer of the following securities is taxed separately from other incomes.

- (a) Stocks (including the right to become a stockholder or an investor, the right to receive an allotment of stocks, and the right to receive stock warrants or an allotment of stock warrants)
- (b) Equities of partners of Limited Partnership (Goshi-Gaisya), General Partnership (Gomei-Gaisya) and Limited Liability Company (Godo-Gaisya)
- (c) Bonds with rights to subscribe new stocks
- (d) Preferential investment
- (e) Beneficiary certificates of private investment trust on securities such as equities
- (f) Beneficiary certificate of certain special purposes trust

Capital gains derived from the transfer of the securities mentioned above

are taxed separately when filing a return. The tax rate applied to these capital gains is 15% (7% from 2003 to 2007 for listed stocks, etc.).

Out of the amount of losses arisen from transfer of listed stocks, etc. from January 1, 2003 onward, those that are not deductible during the relevant year may be carried forward to be deducted within three years thereafter from the capital gains, etc. derived from transfer of stocks.

In addition, there are the following special measures.

- (1) In case the listed stocks, etc. acquired before September 30, 2001 are to be transferred during the period from January 1, 2003 to December 31, 2010, a special treatment for acquisition cost is allowed where the acquisition cost may be regarded by option to be 80% of the price as of October 1, 2001.
- (2) A system (“urgent investment incentive measure”) is granted which may be used in case the listed stocks, etc. purchased by an individual person during the period from November 30, 2001 to December 31, 2002 are transferred from 2005 to 2007, where the capital gains derived from such transfer on the purchase price (the amount of acquisition) less than ¥10 million are not taxed

m. Other Forms of Special Tax Treatment

- (1) If a taxpayer transfers inherited property within three years and ten months of the day of succession, he or she may add the inheritance tax paid on the property to the original acquisition cost in calculating the capital gains arising from the transfer. Furthermore, if a taxpayer transfers inherited land (including the right to use it), he or she may add the inheritance tax paid on all of the inherited land.
- (2) If a taxpayer donates his or her property to the state or local authorities, the capital gains on such property is not taxable. If the property is donated to a benevolent corporation, similar treatment is allowed provided the corporation meets requirements from the viewpoint of the public interest.
- (3) If a taxpayer transfers a national treasure, important cultural asset, or cultural asset designated by the Ministry of Education, Culture, Sports, Science and Technology, the capital gains on such properties are not taxable.

7. Special Tax Treatment of Miscellaneous Income, etc.

- (1) Gains arising from transactions of futures made during the period from January 1, 2003, onward and after the balance is settled are taxed separately from other gains. If losses are generated, the losses remaining after

deductions are made in the relevant year may be subject to deferred deductions in the three years beginning with the year following the year of the transaction from the miscellaneous incomes, etc. obtained from transactions of futures.

- (2) Anti-tax haven measures introduced in the 1978 Tax Reform are applied for individuals or unincorporated business as well as corporations. (For details, refer to the corresponding sections of Chapter III.)

8. Nontaxable Income

Income Tax Law and other related laws specify that several income items are to be exempted.

Some of the principal exempted items are:

- (1) Interest accrued from current bank deposits.
- (2) Interest or distribution of profits from deposits or joint operation trusts which students of schools such as primary schools, junior high schools, or senior high schools or similar institutions excluding universities make or entrust under the instruction of the head of such schools.

[Items (3) to (5) apply to single parent households, and the physically handicapped.]

- (3) Interest accrued from postal savings not exceeding ¥3.5 million. Because of the privatization of Japan post, this exemption will be abolished in October 1, 2007.
- (4) Interest income from small deposits,
 - (a) Interest or distribution of profits from deposits, joint-operation trusts, bonds and debentures, open-end bond investment trusts, is exempt from tax if the principal does not exceed ¥3.5 million.
 - (b) A taxpayer who intends to apply for this exemption is required to submit at the time he or she makes the investment a “Small Savings Tax Exemption Form” to the Director of the Tax Office through the office or branch of the financial institution handling the investment.
- (5) Interest on central and local government bonds, not exceeding ¥3.5 million. Procedures similar to the one outlined in (4) (b), above must be followed for the taxpayer to receive this exemption. This exemption is intended to encourage the purchase of government bonds by individuals.
- (6) Interest income or distribution of profits deriving from Savings Contracts for the Formation of Employees’ Assets Regarding Acquisition of Principal Residential Accommodations or from Savings Contracts for the Formation of Employees’ Assets Regarding Pension Plans.

Under the System for Savings for the Formation of Employees’ Assets,

interest or other proceeds from specific deposits, postal life insurance, special types of life insurance, postal life insurance or mutual-aid life insurance, joint operation trusts, bonds and debentures, open-end bond investment trusts that employees acquire with respect to deposits, payment of installments, or premiums to be withheld from their salaries under Savings Contracts for the Formation of Employees' Assets Regarding Acquisition of Principal Residential Accommodations or Savings Contracts for the Formation of Employees' Assets Regarding Pension Plans, shall be exempt from tax so long as the total principal does not exceed ¥5.5 million. A taxpayer who intends to apply for this exemption is required to follow procedures similar to those required for the exemption of small savings.

- (7) Interest from the tax payment deposits.
- (8) Pensions and similar payments to persons disabled in the course of discharging official functions or business duties; pensions and annuities for bereaved families (only in connection with services rendered by the deceased), and payment made through local authorities' mutual aid programs for physically handicapped or mentally retarded persons.
- (9) A reasonable amount for travel expenses paid to employees (those with employment income) for business trips and for relocations due to a change of post, new employment, or retirement
- (10) A reasonable amount for transportation expenses paid to employees (those with employment income) for commuting between their residence and workplace
- (11) Payments in kind (meals and clothing, etc.) that are indispensable for the discharge of the employee's duties
- (12) Overseas allowances paid to diplomats, etc., who are deemed to be resident of Japan while staying abroad
- (13) Salaries, wages, bonuses, or similar remuneration for services rendered by a government official of a foreign country or a local public entity thereof, or an official of certain international institutions designated by the Minister of Finance are exempt from tax on the basis of reciprocity, unless the person is a Japanese national or has the immigration status of a permanent resident in Japan, provided that such services are not rendered in connection with profit making activities.
- (14) Economic benefit concerning low interest loans provided by employers to their employees for the acquisition of their own residence.
- (15) Income from the transfer of movable property for daily living.
- (16) Capital gains from the compulsory conversion of assets of bankrupt entities by tax authorities, etc. into money.
- (17) Income from the sale of bonds, bond investment trusts and beneficiary

Income Tax (Individual Income Tax)

certificates of loan trusts.

- (18) Amounts received in cash or in an assimilated form for scholastic achievement, such as the Nobel Prize or a grant for certain educational, artistic, or scientific purposes.
- (19) Certified rewards for the records of the Olympic Games provided by the Japan Olympic Committee
- (20) Amount received by inheritance, bequest, or donation from an individual
- (21) Proceeds of injury insurance, compensation, or consolation money for mental or physical injuries
- (22) Proceeds from casualty insurance or compensation for accidental damage to property (excluding amounts for the loss of prospective business profits caused by damage to inventory or other business assets)
- (23) Money donated by corporations to election campaigns in accordance with the Public Office Election Law
- (24)* Insurance payments under the Health Insurance Plan
- (25)* Insurance payment under the Unemployment Insurance Plan
- (26)* Livelihood allowances granted under the Daily Life Protection Law, etc.
- (27) Allowances received as Imperial Court expenses or Imperial Household expenses in accordance with the provisions of the Imperial Household Law
- (28) Payments in money or in kind for school expenses (except payments in the nature of wages or remuneration) and maintenance allowances paid by persons responsible for the support of the recipient
- (29) Economic benefit from stock acquisition by exercising subscription right, etc, (stock option) given to specific directors, etc.

9. Aggregation of Income and Treatment of Profits and Losses

Taxable income can be divided into three broad categories : (1) ordinary income, (2) timber income, and (3) retirement income. Ordinary income consists of income of a recurring nature (interest income, dividend income, real estate income, business income, employment incomes and miscellaneous income) and of income of a temporary nature (capital gains and occasional income). Timber income and retirement income are taxed separately from other types of income, but any losses in timber income may be offset first with respect to profits from other items of income of a recurring nature; then, if the difference is still negative, with respect to profits in items of a temporary nature, and finally with respect to retirement income.

As a special measure, interests and dividends below may be taxed separately

* Exempted item prescribed in neither the Income Tax Law nor the Special Taxation Measures Law.

from other income under the Special Taxation Measures Law (see 2/5,1).

- (1) Interest on ordinary deposit and other deposits of a similar nature are taxed at the source at the rate of 15% and are excluded from taxable income when filing a return.
- (2) Distributions of profits from privately-subscribed bond investment trusts receivable etc, may be taxed separately at the source at the rate of 15%.
- (3) Dividends (excluding the distribution of profits from a privately-subscribed bond investment trust etc,) distributed by the listed corporations are taxed at the source at the rate of 15% (7% for dividends distributed during the period between April 2003 and March 2008), and the taxpayers can decide whether they file it or not.

Capital gains on land, buildings, or the right to use land are taxed separately from other income.

Capital losses (excluding capital losses on land, buildings, or the right to use land, and capital losses on securities such as stocks, etc) may be offset against profits from the following incomes: occasional income; profits from income of a recurring nature; timber income and; retirement income.

Losses incurred in real estate income (of the interest on loans made to acquire such real estate that yields real estate income, that concerning the acquisition of land is excluded) or business income may be offset against profits from the other items of income: income of a recurring nature; income of a temporary nature; timber income and; retirement income.

Losses incurred in dividend income, occasional income, miscellaneous income, and capital gains from properties not necessary for ordinary livelihood cannot be offset against profits from other incomes.

10. Carryover of Losses

- (1) The amount of net losses (which cannot be completely deducted by the procedures described in the previous section 9) and which cannot be completely deducted among the losses described in 2/4, 1 (the amount of casualty losses) are not deductible.

Undeductible losses can be carried over for up to three years provided that the taxpayer files a return in which the nature of the losses is identified.

Administrative procedures required for this carryover vary according to the type of return filed in the year when the loss arose.

a. Taxpayers Filing a White Return

- (1) Losses with respect to writing, composition of music, and fishing (losses connected with fluctuating income), or losses to inventory due to

a natural disaster or other business assets can be carried over for up to three years. Other net losses cannot be carried over.

- (2) The non-deductible balance of a casualty loss may be carried over for up to three years.

b. Taxpayers Filing a Blue Return

Both the net losses and miscellaneous income losses explained above may be carried over for three full years.

- (2) In case capital losses from the transfer of listed stocks remain after their deduction from capital gains from transfer of stocks in the relevant year, these may be subject to a deferred deduction for the remaining losses under certain conditions. The deductions are to be made within three years beginning with the year following the relevant year of the transfer.
- (3) If a resident or a nonresident who has a permanent establishment in Japan acquires stocks of venture businesses that meet certain requirements and incurs losses by transferring them before they are listed, the amount that cannot be completely deducted from the capital gains for the year derived from the sale of stocks can be carried over and deducted from capital gains for the next three years under certain conditions.
- (4) If an individual incurs capital losses derived from the transfer of a residential property, the losses can be carried over and deducted from the gross income of the next three years (limited to years in which total income is ¥30 million or less) under certain conditions.
- (5) Out of the losses generated by settling the balance of transactions of futures, if losses still remain after deductions from the miscellaneous incomes, etc. obtained from transactions of futures for the year of the settlement, they may be subject to deferred deductions from the miscellaneous incomes, etc. obtained from transactions of futures each year within the next three years, based on certain requirements.

11. Carryback of Net Losses

Taxpayers filing blue returns both in the current and in the previous year are allowed to carry back the amount of net losses for one year. The amount of income tax in previous year is recalculated, and the difference between tax paid in previous year and tax recalculated is returned.

2/4 Income Deductions

The following deductions and exemptions are allowed when calculating taxable ordinary income, taxable retirement income, or taxable timber income. These deductions and exemptions are made first from ordinary income and next from timber income, and finally from retirement income, if there is any residual sum.

1. Deduction for Casualty Losses

If a resident taxpayer has a loss on assets (excluding inventory or other business assets and properties not necessary for ordinary livelihood) from a disaster etc. for himself or herself, the spouse living with him or her or other relatives, or unusual expenditures due to an earthquake, storm, fire, theft, or usurpation, etc., and the portion of such a loss that is not recovered by insurance proceeds, etc., exceeds 10% of the total of ordinary income retirement income and timber income, the excess amount is deductible from ordinary income, retirement income, or timber income (as for expenses directly caused by a disaster, 10% of the total of all income or ¥50,000). As to losses incurred during the three preceding years, before previous year (excluding the losses deducted before previous year) may be deducted only when the taxpayer had continuously been filing returns, whether blue or white.

2. Deduction for Medical Expenses

If a resident taxpayer pays medical or dental fees for oneself or a spouse living together with the taxpayer or other relatives, and the amount of such expenses (minus any insurance proceeds) exceeds the lesser of ¥100,000 or 5% of the total of ordinary income, retirement income, and timber income, the excess amount is deductible from ordinary income, retirement income, or timber income. The maximum deductible amount is ¥2 million.

3. Deduction for Social Insurance Premiums

If a resident taxpayer pays social insurance premiums for oneself or for a spouse living together with the taxpayer or other relatives, that amount is deductible from his or her ordinary income, retirement income, or timber income.

4. Deduction for Small-scale Enterprise Mutual Aid Premiums, etc.

If a taxpayer pays mutual aid premiums for a contract (under which proceeds are paid only upon the termination of the enterprise) with the Small-scale Enterprise Mutual Aid Programs or with Physically Handicapped or Mentally Retarded

Income Tax (Individual Income Tax)

Persons Mutual Aid Programs operated by local authorities, or if a taxpayer pays private pension insurance premiums in accordance with the defined contribution pension plan law, the amount paid is deductible from his or her ordinary income, retirement income, or timber income.

5. Deduction for Life Insurance Premiums

- (1) If a resident taxpayer pays insurance premiums on life insurance contracts, under which the recipient of insurance proceeds is himself or herself, a spouse, or other relatives living with the taxpayer, a portion, up to the maximum indicated below, is deductible from ordinary income, retirement income, or timber income.

Premiums Paid		Deduction
Over	Not over	
	¥25,000	Total amount of premiums paid.....(*)
¥25,000	¥50,000	$(*) \times 1/2 + ¥12,500$
¥50,000	¥100,000	$(*) \times 1/4 + ¥25,000$
¥100,000	–	¥50,000

- (2) If a resident taxpayer pays insurance premiums on a personal pension plan contract where the recipient of the pension payment is the individual or a spouse under specific conditions, a portion, up to the maximum indicated below, is deductible from ordinary income, retirement income, or timber income besides (1).

Premiums Paid		Deduction
Over	Not over	
	¥25,000	Total amount of premiums paid.....(*)
¥25,000	¥50,000	$(*) \times 1/2 + ¥12,500$
¥50,000	¥100,000	$(*) \times 1/4 + ¥25,000$
¥100,000	–	¥50,000

6. Deduction for Casualty Insurance Premiums

If a resident taxpayer pays insurance premiums for fire or other casualty insurance on residence, which is owned by a taxpayer, spouse living with the taxpayer, or other relatives and used for their daily lives, or on household goods necessary for daily living, a portion up to the maximum indicated below is deductible from ordinary income, retirement income, or timber income.

Type of Insurance	Premiums Paid	Deduction
Long-term insurance	Over	Total amount of premiums paid... (1) (1) $\times 1/2 + ¥5,000$ ¥15,000
	Not over	
	¥10,000	
	¥20,000	
Short-term insurance	¥2,000	Total amount of premiums paid... (2) (2) $\times 1/2 + ¥1,000$ ¥3,000
	¥4,000	
	¥2,000	
	¥4,000	

Note) It is revamped to the “deduction for earthquake insurance premium” in 2007. The amount of insurance premium corresponding to earthquake-induced damages in a casualty insurance contract (maximum 50,000 yen) is deducted from the income.

7. Deduction for Contributions or Donations

As for contributions or donations by a taxpayer to (i) the state or local authorities, (ii) designated donations, (iii) specified corporations for improving public interest, (iv) certain non-profit organizations that are certified by the Commissioner of the National Tax Agency and (v) political organizations which satisfy certain conditions, an amount in excess of ¥5,000 is deductible from ordinary income, retirement income, or timber income up to an amount equal to 30% of the total of ordinary income, retirement income, and timber income.

8. Exemption for the Handicapped

If a resident taxpayer is handicapped or has a handicapped spouse or dependent, ¥270,000 for each handicapped individual is deductible from ordinary income, retirement income, or timber income. An exemption of ¥400,000 is provided for a person who has a special handicap.

9. Exemption for Widows, Widowers, or Working Students

If a resident taxpayer is a widow living with child(ren) as dependent(s) or having income not exceeding ¥5 million, or a widower living with child(ren) as dependent(s) and having income not over ¥5 million, or a working student whose income is not over ¥650,000, ¥270,000 is deductible from ordinary income, retirement income, or timber income. A widow satisfying both conditions mentioned above may deduct ¥350,000 from ordinary income, retirement income, or timber income.

10. Exemption for Spouses

The following exemption is available to a resident living with a spouse on condition that the spouse's income does not exceed ¥380,000.

[status of the spouse]

- a. those not falling under category b ¥380,000
- b. 70years or older..... ¥480,000

[Note] In case where the spouse is a Special Handicapped Individual living with the taxpayer, an additional exemption of ¥350,000 is available in both categories.

11. Special Exemption for Spouses

In case where a resident whose annual income does not exceed ¥10 million and is living with a spouse whose income exceeds ¥380,000 and is not less than ¥760,000 (the amount exceeds ¥1,030,000 and not less than ¥1,410,000 for employment income before deduction,), the taxpayer is entitled to deduct a certain amount corresponding to the spouse's income from the taxpayer's own income.

The Special Exemption for Spouses was introduced to settle the so-called “part-time worker problem” in the tax amendments for September 1987. The pre-amendment tax law stipulated that where a spouse's employment revenue exceeds a certain amount (the amount was ¥900,000 then though it is currently ¥1,030,000), the Exemption for Spouses (¥330,000 then and ¥380,000 currently) is not applied, thereby increasing the tax burden of the wage earner. However the spouse is also made subject to income tax as he or she has become an in-dependent taxpayer regarding income tax. Consequently, the net after – tax receipt of the household as a whole decreases, thereby giving rise to the reversal of the net after-tax receipt. This is the “part-time worker problem”.

The Special Exemption for Spouses is designed in the form of a diminishing deduction; the deductible amount diminishes as the spouse's income increases.

The introduction of the Special Exemption for Spouses solved the problem of part-time worker in which the net after-tax receipts of the household were reversed. The part of the special exemption for spouses, which is applied in addition to the exemption for spouses, was abolished in the tax reform conducted in FY2003.

12. Exemption for Dependents

The term “dependent” is as follows: relatives (except spouses) who are supported by a taxpayer in the same household and meet the condition mentioned in above Section 10. The following exemptions are available for them. The deter–

mination whether a person is qualified a dependent relative is made on the basis of the state of 31 December (or the date of death in case the person is dead).

- a. For each dependent relative ¥380,000
(excluding those falling under b. and c.)
- b. For each elderly dependent relative..... ¥480,000*
(70 years or older)
- c. For each specific dependent relative ¥630,000**

[Note] In case where the dependent relative is a Special Handicapped Individual living with the taxpayer, an additional exemption of ¥350,000 is available in each category.

13. Basic Exemption

A taxpayer is entitled to an exemption of ¥380,000.

2/5 Calculation of Tax Amounts

1. Tax Rates

Income tax due is calculated by applying tax rates to ordinary taxable income, taxable retirement income, or taxable timber income.***

Individual Income Tax Rates

Taxable Income		Tax Rate(%)	Cumulative Tax for Each Bracket
(A)		(B)	(C)
Over	Not over		
–	¥3,300,000	10	–
¥3,300,000	¥9,000,000	20	¥330,000
¥9,000,000	¥18,000,000	30	¥1,470,000
¥18,000,000		37	¥4,170,000

Note: Tax liability is obtained by multiplying the excess amount (A) by the rate (B) and adding the amount (C). For example, income tax due on taxable income of ¥10 million is :

$$(\text{¥10,000,000} - \text{¥9,000,000 (A)}) \times 0.3 \text{ (B)} + \text{¥1,470,000 (C)} = \text{¥1,770,000}$$

* ¥580,000 if living with elderly dependent of lineal ascendance.

** A specific dependent is a dependent from 16 to 22 years old.

*** In the case of timber income, the tax rate is applied to one-fifth of the taxable timber income (see, 2/5, 2).

Individual Income Tax Rates (From FY 2007)

Taxable Income (A)		Tax Rate(%) (B)	Cumulative Tax for Each Bracket (C)
Over	Not over		
–	¥1,950,000	5	–
¥1,950,000	¥3,300,000	10	¥97,500
¥3,300,000	¥6,950,000	20	¥232,500
¥6,950,000	¥9,000,000	23	¥962,500
¥9,000,000	¥18,000,000	33	¥1,434,000
¥18,000,000		40	¥4,404,000

Note: Tax liability is obtained by multiplying the excess amount (A) by the rate (B) and adding the amount (C). For example, income tax due on taxable income of ¥10 million is :

$$(\text{¥10,000,000} - \text{¥9,000,000 (A)}) \times 0.333 \text{ (B)} + \text{¥1,434,000 (C)} = \text{¥1,764,000}$$

In accordance with the Special Taxation Measures Law, interest income is taxed separately. A part of dividends are taxed separately at the option of the taxpayer right to use land. In accordance with the Special Taxation Measures Law, capital gains on land, buildings, and securities are taxed separately (see 2/3, 6).

The tax rates applicable to income from the sale of land, etc., are mentioned in 2/3, 6. d.

2. Taxation on Timber Income

If a taxpayer has income from the sale or transfer of timber, such taxable income is divided by five and the amount of tax due on that amount is multiplied by five to obtain the total tax due.

3. Averaging Taxation on Fluctuating and Extraordinary Income

“Fluctuating income” includes income from: a) fisheries; b) the harvest of certain kinds of seaweed; c) compensation for manuscripts and musical compositions and; d) royalties for copyrights. “Extraordinary income” includes such income as: a) lump sum payments received by professional baseball players, etc., for services to be rendered over three years or longer (the lump sum should be more than double the yearly amount of remuneration) and; b) a lump sum payment received by an owner of immovable property, ships, aircraft, patents, etc., for the lease of such properties for three years or longer (the lump sum amount should be more than double the yearly amount of rent, royalties, etc.). If a

taxpayer has such fluctuating income* and extraordinary income, the sum of which is not less than 20% of his aggregate or her income in the year, the amount of tax on this income may be computed by the “averaging taxation” method. A taxpayer must clearly indicate the use of this method on the final return. By this method, four-fifths of the total of the fluctuating income (or the amount exceeding one-half of the sum of the fluctuating income in the preceding two years) and extraordinary income is excluded from taxable income. The average tax rate applicable to the remaining taxable income is applied to four-fifths of the amount so excluded to obtain the total due tax. The purpose of the “averaging taxation” method is to alleviate the heavy tax burden that might result from application of progressive tax rates to these kinds of special income.

4. Tax Credits

Under present tax legislation, the following income tax credits are primary examples of those allowed:

a. Credit for Dividends

The Income Tax Law allows a taxpayer to deduct 10% of dividend income from income tax. However, if ordinary taxable income, including dividends, exceeds ¥10 million, a tax credit of only 5% is applicable to the fraction of dividend income equal to the ordinary taxable income minus ¥10 million, and that of 10% is applicable to remaining dividend income.

In the case of distribution of profits from securities investment trusts, 5% of such distribution income may be deducted from income tax. If taxable ordinary income exceeds ¥10 million, 2.5% of that distribution income, which is equal to the ordinary taxable income minus ¥10 million, is deductible.

b. Credit for Foreign Taxes

- (1) Foreign income taxes of residents may be credited against their Japanese income tax liability. Foreign income tax (including foreign local taxes on income) is deductible from Japanese income tax due for the tax year in which such foreign income tax is to be paid, subject to the following overall limitation:

* In respect to “fluctuating income,” it is subject to the “averaging taxation only when it exceeds one-half of the total “fluctuating income” in the preceding two years.

Income Tax (Individual Income Tax)

Japanese income tax \times

$$\frac{\text{Total income from sources outside Japan* (Foreign income)}}{\text{Entire income subject to Japanese income tax}} \\ (\text{income from foreign and domestic sources})$$

- (2) When foreign taxes exceed the limitation mentioned in (1) above, the excess amount of foreign taxes may be carried over for three succeeding years. On the other hand, when the limitation of credit exceeds the foreign taxes to be paid, the excess amount may be carried over up to three years.
- (3) Foreign income tax incurred may, at the taxpayer's option, be deducted from taxable income as necessary expenses. If a resident taxpayer decides to use the foreign tax credit, foreign income taxes cannot be deducted as necessary expenses. In this case, the taxpayer must include in the taxable income the total amount of foreign taxes paid each tax year.

c. Credit for Housing Loans

A taxpayer who constructs, purchases, enlarges, or rebuilds a house, financing its cost with housing loans, and uses it as his or her own dwelling is entitled to an income tax credit up to the maximum described below, for 10 years after the year in which residence in the house commenced under specific conditions such as more than half of the floor space of 50 m² or greater being used as his or her own dwelling. The tax credit base is equal to the amount of the housing loans calculated at the end of each year, and loans obtained not only from private financial institutions but also from public institutions.

The deductible period and the rates for tax credits correspond to the year in which residence in the house commenced as follows:

* (a) In computing total income from sources outside Japan, a net loss incurred in a foreign country may not be taken into account at the taxpayer's option.
(b) The entire income subject to Japanese income tax is the amount before deduction of the losses carried over from previous tax years.
(c) The figures in this formula are for the tax year in which the foreign income is taxed.

Income Tax (Individual Income Tax)

Residence started in 1999 or 2000, or started from 1 January to 30 June in 2001		Residence started from 1 July in 2001 to 31 December in 2004		Residence started from 1 January 2005 to 31 December 2005	
Deductible Period	15 years	Deductible Period	10 years	Deductible Period	10 years
Tax Credit Rate		Tax Credit Rate		Tax Credit Rate	
If the remaining housing loan balance at the end of the year (R.H.L.B.) is ¥50 million or less:	The R.H.L.B. \times { 1.0% (for the first 6 years) 0.75% (for the next 5 years) 0.5% (for the last 4 years)	If the R.H.L.B. is ¥50 million or less	The R.H.L.B. \times 1.0%	If the R.H.L.B. is ¥40 million or less	The R.H.L.B. \times { 1.0% (for the first 8 years) 0.5% (for the last 2 years)
Maximum tax credit amount (for each year)	{ ¥500,000 (for the first 6 years) ¥375,000 (for the next 5 years) ¥250,000 (for the last 4 years)	Maximum tax credit amount (for each year)	¥500,000	Maximum tax credit amount (for each year)	{ ¥400,000 (for the first 8 years) ¥200,000 (for the last 2 years)
Maximum tax credit amount (for the deductible period in total)	¥5,875,000	Maximum tax credit amount (for the deductible period in total)	¥5,000,000	Maximum tax credit amount (for the deductible period in total)	¥3,600,000

Residence started from 1 January 2006 to 31 December 2006		Residence started from 1 January 2007 to 31 December 2007		Residence started from 1 January 2008 to 31 December 2008	
Deductible Period	10 years	Deductible Period	10 years	Deductible Period	10 years
Tax Credit Rate		Tax Credit Rate		Tax Credit Rate	
If the R.H.L.B. is ¥30 million or less	The R.H.L.B. \times { 1.0% (for the first 7 years) 0.5% (for the last 3 years)	If the R.H.L.B. is ¥25 million or less	The R.H.L.B. \times { 1.0% (for the first 6 years) 0.5% (for the last 4 years)	If the R.H.L.B. is ¥20 million or less	The R.H.L.B. \times { 1.0% (for the first 6 years) 0.5% (for the last 4 years)
Maximum tax credit amount (for each year)	{ ¥300,000 (for the first 7 years) ¥150,000 (for the last 3 years)	Maximum tax credit amount (for each year)	{ ¥250,000 (for the first 6 years) ¥125,000 (for the last 4 years)	Maximum tax credit amount (for each year)	{ ¥200,000 (for the first 6 years) ¥100,000 (for the last 4 years)
Maximum tax credit amount (for the deductible period in total)	¥2,550,000	Maximum tax credit amount (for the deductible period in total)	¥2,000,000	Maximum tax credit amount (for the deductible period in total)	¥1,600,000

5. Proportional Tax Credit

As for income tax from 1999 to 2005, the amount of the proportional tax credit (20% of the tax amount before the proportional tax credit (up to: ¥250,000)) is deducted from the tax amount before the proportional tax credit. In the FY2005 tax reform, half of the benefits of the proportional tax credit was reduced. The rate of the tax credit was reduced from 20% to 10% and the ceiling on the tax credit was reduced from ¥250,000 to ¥125,000 (Applicable for CY2006).

The proportional tax credit was abolished in FY2006 tax reform (Applicable from 2007).

2/6 Payment of Income Tax

1. General

Income tax is paid by self-assessment unless it is withheld at the source. Income tax on wages, salaries, interest, dividends, etc., is withheld by payers of such income, who remit withholding tax of the government on behalf of the taxpayer. Under the self-assessment system, each taxpayer is required to file a return and pay the amount of tax due at the same time. The amount withheld is treated as an advance payment of tax payable by the recipient of the income.

Income is taxed on a calendar year basis. A return is to be filed for the annual income no later than 15 March of the following year, and the tax due remitted at the same time. However, if the income tax self-assessed for the previous year exceeds a fixed amount, about two-thirds of the total tax calculated on the basis of ordinary income of the preceding year is prepaid in two equal installments no later than 31 July and 30 November. The difference between actual tax due and the prepayment amount should be paid when filing a return by 15 March of the following year.

The prepayment of tax made on or before 31 July and 30 November is called an “Estimated Payment”. The return due no later than 15 March of the following year is called the “Final Return.”

2. Keeping Proper Records

- (1) An individual who has income from business, real estate, or timber is required to keep records and source documents for seven years in principle after filing a final return or submitting the report on Gross Income.
- (2) An individual who has income of more than ¥3 million from business, real estate, or timber in the previous year or the year before last, is required to keep records of this business activity in a simple form.

- (3) When examining the taxpayer's income, tax officials may inspect the books kept by the taxpayer.
- (4) An individual who receives the approval for a blue return, however, shall be subject to different requirements regarding the keeping of records (see 2/7).

3. Estimated Payment

As a rule, those whose estimated tax due in a year amounts to ¥150,000 or more must make estimated tax payments during the year and are notified of this by the tax authorities. The estimated tax due is, in short, the tax on total taxable income less the tax withheld in the preceding tax year.

In calculating total taxable income, any income of a temporary nature (such as capital gains, occasional income, miscellaneous income, and extraordinary income not falling under the category of miscellaneous income) is excluded.

The amount of each prepayment, on 31 July and 30 November is one-third of the estimated tax due.

Special treatment is given to "special farm income-earners." A special farm income-earner is an agricultural income-earner whose income from agriculture is no less than 70% of his aggregate income and who earns at least 70% of the income after 1 September. In the case of the special farm income-earner, one-half of the estimated tax is to be paid by 30 November with the remainder to be paid when filing the final return.

The tax prepayment method is based on the assumption that the current income of a taxpayer will not change materially from the previous year. If it is likely that income will decrease in the current year from the previous year's level, a taxpayer is allowed to calculate the estimated tax on the estimate of income for the current year.

Application for reduction of the prepayment amount shall be made on or before 15 July or 15 November on the basis of estimated income for the current year as of 30 June and 31 October respectively. Special farm income-earners, however, can make application only on or before 15 November on the basis of the 31 October estimate. Applications will be accepted if the estimated tax for the current year is expected to be below the actual tax of the previous year because (1) the taxpayer terminated or suspended business operations, (2) unusually large medical expenses were incurred, or (3) the number of his or her dependents increased. In any case, the tax authorities have the right to approve or disallow the application based on an investigation.

4. Final Returns

A resident taxpayer is required to file a final return, unless (1) his or her total

Income Tax (Individual Income Tax)

income does not exceed income deductions or (2) his or her tax due is less than the credit for dividends to which he or she is entitled.

As a result, the resident taxpayer may at his or her option exclude dividends derived from listed stocks, etc. from income as described earlier (see 2/3,9).

Final returns should be filed with the appropriate tax authority by 15 March of the following year. The documents that explain the gross income and deductible expenses should be attached to the final return (for blue returns, see 2/7, 2).

A taxpayer whose salary is ¥20 million or less need not file a return if (1) he or she earns, no more than ¥200,000 other than the salary he or she receives from the employer, or (2) he or she receives salaries, wages, etc., from two or more employers, and his or her income from salaries, wages, etc., after deductions for social, life, and fire or other casualty insurance premiums, and exemptions for spouse, dependents, physically handicapped individuals, widows, and working students does not exceed ¥1,500,000 and his or her other income is ¥200,000 or less. If the amount of tax withheld or prepaid during the tax year exceeds the amount of tax calculated for the total income of the year, a taxpayer may file for a refund. A taxpayer may file an amended return if he finds there is any deficiency in his original return. In this case, he should immediately remit the amount of the deficiency. If a taxpayer finds his actual amount of tax is less than the amount reported in his original return, he may request correction within a year after the last day of the filing period.

A taxpayer may also file a final return even after the due date unless he or she receives tax determination by the tax authorities. In this case, he or she should immediately pay the amount of tax reported on the return.

5. Assessment in the Event of Failure to File Correct Returns

If the facts and figures stated in the return differ from those determined upon examination, the Director of the Tax Office shall, at his or her own discretion, correct the amount of tax and other related items.

If an individual who is required to file a return has failed to do so, the Director of the Tax Office after investigation shall determine the amount of the individual's income and other related items.

The Director of the Tax Office may correct amounts that were previously corrected or determined when it is discovered that, based upon investigation, there is still a deficiency in these amounts. When a notice of correction or determination is issued, the taxpayer must pay the amount given in such a notice within one month from the date of issue.

2/7 Blue Returns

1. General

The blue return system is intended to improve taxpayer's bookkeeping and encourage honest self-assessment. When the self-assessment system was introduced, a large number of taxpayers did not follow modern accounting practices, nor did they keep proper accounting records. To assure the success of the self-assessment system, improvement of taxpayers' accounting practices was of vital importance. To this end, those who maintain proper accounts as required under the blue return system and report their income correctly based on those books and records are given certain privileges, as mentioned in item 3 below.

2. Approval by the Director of the Tax Office

An individual who has income from business, real estate, or timber and who keeps proper accounting records* may file a blue return if he or she submits an application by 15 March and obtains the approval of the tax authorities by the end of that year. Once a taxpayer obtains approval, he or she is entitled to file a blue return for all subsequent years. The Director of the Tax Office will approve the application on the condition that the taxpayer's books are kept in accordance with official requirements. The blue final return must be filed together with the balance sheet, income statement, and other documents indicating the items necessary for calculating the taxpayer's income.

3. Privileges

Main privileges granted to an individual taxpayer filing a blue return include:

- a. The taxpayer is allowed as expenses an amount for wages or income deemed reasonable if paid to relatives living with him or her in the same household (family employees) (see 2/3, 3.b.(3)).
- b. The taxpayer is entitled to a special deduction for a blue return (see 2/3, 3.c).
- c. A deduction is allowed for amounts credited for various tax-free retentions such as reserves for bad debts, loss on returned goods unsold, and retirement allowances (see 2/3, 3.b.(4)~(6)).
- d. The following measures are allowed to take; special income tax credit for

* Taxpayers may use a simplified accounting system in lieu of the complete accounts required for eligibility to file a blue return. The simplified accounts consist mainly of a cash-book and sales and purchase records. In addition, taxpayers who have income no more than ¥3 million from real estate and business income before deducting salaries to family employees for the year before the last tax year may use the simpler cash-basis accounting method (see 3. g below).

Income Tax (Individual Income Tax)

incremental research and development expenses (special tax credit for research and development starting in 2007), special depreciation in specific equipment, additional depreciation of specific medical-use buildings, reserve for the prevention of mineral pollution of metal mining, and special deduction for prospecting for new mineral deposits. (see 2/3, 3. b.(7)).

- e. Net losses may be carried over to offset income for three succeeding years and may be carried back to offset the income of one preceding year (see 2/3, 10 and 11).
- f. The Director of the Tax Office may correct the income of a taxpayer filing a blue return, excluding certain exception, only when errors are found in the calculation of taxable income based on the taxpayer's books and records. As a result, the Director of the Tax Office, in making corrections of the tax amount, should attach a statement explaining the grounds for the correction.
- g. A taxpayer earning ¥3 million or less in income from real estate and business incomes before deducting salaries to family employees in the tax year before last may calculate his or her income on a cash basis instead of an accrual basis.

2/8 Withholding Income Tax at the Source*

1. General

Those who pay salaries, wages, interest, dividends and other income specified by the Income Tax Law are required to withhold income tax and remit the amount to the government before the 10th of the month following the month in which the payment was made. Those who employ only one or two housekeepers, however, are not required to withhold income tax on salaries paid to housekeepers.

The Director of the Tax Office will issue a notice of payment to those who fail to withhold or to remit amounts so withheld. Withholding is in effect a prepayment of income tax or corporation tax; tax withheld at the source is added to the taxpayer's final liability for the year.

2. Interest and Dividend Income

Interest paid to residents is normally subject to withholding at the source at the rate of 15% (a 5% local inhabitants tax is levied in addition). Dividends** (except the distribution of gains from privately-subscribed bond investment trusts, etc.) paid to residents are normally subject to withholding at the source at a rate of 20%. The total tax (national and local) on dividends derived from listed com-

* For withholding required on payments to nonresidents, see 24/1, 6.

** Dividend not paid within one year after approval of payment by a general stockholders meeting, etc., shall nevertheless be subject to withholding tax one year after such approval of payment.

panies is withheld at the rate of 10% from 1 April 2003 to 31 March 2008. The distribution of gains from privately-subscribed bond investment trusts, etc. is subject to withholding at the source at a rate of 15% (a 5% local inhabitants tax is levied in addition). Interest or dividends accruing from securities issued outside of Japan are subject to withholding at payment intermediaries at the rate of 15% or 20%.

3. Income from Original Issue Discounts on Debentures

In principle, income from an original issue discount on debentures is subject, upon issuance, to a withholding tax rate of 18%.

4. Employment Income

a. Ordinary Salaries

Salaries paid* to residents are subject to income tax withholding at the source. The amount to be withheld may be determined using the “Tax Withholding Table” provided as an attached table to the Income Tax Law according to the nature of the salary, the period of payment, and the number of dependent relatives the income earner has. In order to withhold income tax properly, salary recipients must submit to the tax authorities, through their employer, “a statement concerning the exemption for dependents, etc.” giving the names of dependent relatives and other necessary particulars.

- (1) For salary paid monthly, the tax amount is obtained from the “Monthly Table” according to the amount of salary paid and the number of dependent relatives.
- (2) For salary paid daily, the tax amount obtained from the “Daily Table” according to the amount of salary paid and the number of dependent relatives.
- (3) For salary paid weekly or every ten days, the tax amount is obtained from the “Daily Table” or the “Monthly Table” by converting the amount of salary to the daily or monthly equivalent, respectively.
- (4) For persons paid on a daily basis, the tax amount is determined by the “Daily Table”(Column C).

These Tables, which indicate the amount of tax to be withheld, are formulated in the following manner:

* Normally, income tax must be withheld upon the payment of salaries, wages, etc. When bonuses payable to directors has not been paid within one year after approval for payment by a general stockholders meeting, etc., such bonus is regarded as having been paid one year after such approval, and income tax is payable at that time.

Income Tax (Individual Income Tax)

(a) Monthly Table

$$\{(MS - SIP) \times 12 - (ID + BE + ED)\} \times \text{tax rate} \times 1/12$$

(b) Daily Table

$$\{(DS - SIP) \times 360 - (ID + BE + ED)\} \times \text{tax rate} \times 1/360$$

Excerpts from Monthly Tables (Column A)

(In yen)

Monthly salary after deducting social insurance premiums		Dependent Relatives and Others*					
		0	1	2	3	4	5
Not less than	Less than	Amount of tax					
224,000	227,000	10,010	7,160	4,310	1,460	0	0
227,000	230,000	10,200	7,350	4,500	1,650	0	0
230,000	233,000	10,380	7,530	4,680	1,830	0	0
233,000	236,000	10,570	7,720	4,870	2,020	0	0
236,000	239,000	10,760	7,910	5,060	2,210	0	0
239,000	242,000	10,950	8,100	5,250	2,400	0	0
242,000	245,000	11,140	8,290	5,440	2,590	0	0

(Note) The different tax table (omitted) is applied from January 1, 2007 in calculating the amount of withholding tax from the salary because the Proportional Tax Credit was abolished in FY2006 Tax Reform.

(c) Column C of the Daily Table

$$\{(DS - SIP) \times 264 - (ID + BE + ED^{**})\} \times \text{tax rate} \times 1/264$$

Where

MS: Monthly wages and salaries ID: Employment income deduction

DS: Daily wages and salaries BE: Basic exemption

SIP: Social insurance premium ED: Exemption for spouse and dependents

Since 1967, a special calculation method may be used to facilitate the use of computers.

An example of calculating the withholding tax on salaries by applying the Monthly Table is given below:

Amount of monthly salary	¥250,000
Social insurance premiums	¥17,500
Number of spouse and dependent relatives	3 persons

* "Others" means handicapped persons, widows, and working students for the purpose of exemption.

** ED of Column C of the Daily Table is fixed at the amount calculated on the assumption that a daily worker has a spouse and two children.

In this case, the tax amount is ¥1,830, found in the above table at the intersection of the line showing a net salary (after deducting social insurance premiums) of ¥232,500 and the column for three dependents.

b. Bonuses

The withholding rate applicable to bonuses is obtained from the Rate Table based on the recipient's salary in the preceding month, the number of dependents, etc. For employees who did not receive a salary in the preceding month, the withholding tax is obtained by (1) dividing the bonus by 6 or 12 (the number of months on which the bonus is based), (2) determining the withholding tax on this amount by reference to the Monthly Table, and (3) multiplying this tax amount by 6 or 12, respectively.

The "Rate Table," which is applied in calculating the withholding tax on bonuses, is calculated as follows:

$$\begin{aligned} & [(MS \times 17^*) - (ID + BE + ED)] \times \text{tax rate} - \{(MS \times 12) \\ & \quad - (ID + BE + ED)\} \times \text{tax rate} \div (MS \times 5) \end{aligned}$$

An example of calculating the withholding tax on a bonus is where:

Amount of salary in the preceding month	¥250,000
Social insurance premiums deducted from this salary	¥17,500
Number of dependents	two persons
Amount of bonus	¥400,000

Excerpts from Rate Tables (Column A)

(In thousand yen)

Rate to be applied to the amount of the bonus (%)	Dependents and Others					
	0		1		2	
	Not less than	Less than	Not less than	Less than	Not less than	Less than
0	(less than) 64		(less than) 88		(less than) 122	
2	64	69	88	95	122	136
4	69	75	95	109	136	154
6	75	82	109	349	154	378
8	82	350	349	381	378	407
10	350	385	381	413	407	439
12	385	418	413	447	439	476
14	418	525	447	525	476	525
16	525	698	525	721	525	744
18	698	735	721	759	744	783
20	735	776	759	801	783	826
22	776	821	801	849	826	878
24	821	875	849	906	878	936

* This figure assumes that an ordinary employee receives a bonus amounting to 5 times his or her salary in the preceding month in addition to the total regular salary during the year.

Income Tax (Individual Income Tax)

(Note) The different tax table (omitted) is applied from January 1, 2007 in calculating the amount of withholding tax from the salary because the Proportional Tax Credit was abolished in FY2006 Tax Reform.

In this case, the salary of ¥232,500(after deducting social insurance premiums) falls under the 6% rate in the column reflecting two dependents, so the amount of tax is $¥400,000 \times 6\% = ¥24,000$. If the bonus payment precedes that of ordinary salary in the month when the year-end adjustment is made, tax other than ordinary tax liability on the bonus which is expected to be due as a result of year-end adjustment may be withheld.

c. Year-end Adjustment

Persons employing residents (except those whose salaries exceed 20 million yen and those employed on a daily basis) must make a year-end adjustment when the last payment of the year is subject to withholding tax, whether the last payment is ordinary salary or a bonus. The year-end adjustment is made through the following procedures: (1) determining the total salary paid during the year; (2) determining the tax due on the aggregate salaries (3) comparing the tax due with the tax actually withheld during the year and; (4) withholding the difference in addition to the tax on the last payment, or reducing the tax on the last payment to offset any excess withholding for the year.

Those who employ nonresidents withhold income tax, normally, at the rate of 20% of their salary (see 24/1, 6).

5. Retirement Income

Retirement income is subject to withholding tax.

Normally the amount of the withholding tax is calculated on the basis of the half of the retirement income after subtracting the special deduction for retirement income (see 2/3, 2.(6))

6. Miscellaneous Income from Public Annuities

Public annuities paid to a resident are subject to income tax withholding at the source. Tax withholding is formulated as follows:

$$TW^* = (PP - D^*) \times 10\%$$

$$TW = TW^* - PD$$

$$PD = TW^* \times 10\%$$

(upper limit: $¥10,450 \times M$)

(Note) The amount of withholding tax on public annuities after January 1 2007 is formulated as follows:

$$TW^* = (PP - D^*) \times 5\%$$

Special rule of proportional deduction on public annuities are applied until December 31, 2006 and will be abolished then, because proportional tax credit was abolished in FY2006 tax reform (Applicable from 2007).

TW: Tax withholding

TW*: Tax withholding before proportional tax credit

PP: Payment of public annuities

D*: Deduction

PD: Proportional deduction of public annuities

M: Number of months on which the calculation of public annuities is based

① Fundamental Deduction

Person paid public annuities	
Younger than 65 years old	Max {PP × 25% + 65,000} Min ¥90,000
Not younger than 65 years old	Max {PP × 25% + 65,000} Min ¥135,000

② Personal Deduction

	Contents	Deduction(¥)
Taxpayer	㊶ Handicapped (Severely handicapped)	22,500 (35,000)
Taxpayer with spouse who satisfies 2/4, 11 and dependents	㊷ Taxpayer with spouse (70 years old or older)	32,500 (40,000)
	㊸ Taxpayer with dependent relatives [(i) specific dependent relatives or (ii) dependent relatives of 70 years old or older]	32,500 per capita [(i) 52,500 per capita (ii) 40,000 per capita]
	㊹ Person mentioned in ㊷ or ㊸ is handicapped (severely handicapped)	22,500 per capita (35,000 per capita)

7. Remunerations, Fees, etc.

- a.** The following items are subject to a 10% withholding tax on each payment of up to 1 million yen and 20% for those above ¥1 million (except **b**) :

Income Tax (Individual Income Tax)

- (1) Remuneration for manuscripts, illustrations, music compositions, recordings, designs, broadcasting, and royalties from copyrights (including quasi copyrights) and industrial property; remuneration or fees for lectures, dramatization, translation, proofreading, bookbinding, stenography, and blocks copy; and remuneration or fees for instruction of any kind of sport.
- (2) Fees or other remunerations to lawyers, certified public accountants, accountants, licensed tax accountants, patent attorneys, land surveyors, architects, real estate appraisers, business consultants, building agents, or fire or automobile damage appraisers.
- (3) Fees or other remunerations to professional soccer players, tennis players, baseball players, wrestlers, golfers, bowlers, jockeys, models, racers, bicycle racers, small automobile racers, or motorboat racers.
- (4) Fees or other remunerations for public entertainment such as movies, plays, music, dance, tricks, or acrobatic feats, etc., or performances, production, or plans for broadcasting.
- (5) Fees or other remunerations to the services by hostesses of bars or salons etc.
- (6) Fees* or other remunerations to taxpayers whose business is providing the personal services of public entertainers for their performance.
- (7) Lump sum payments received by professional baseball players, etc., for services to be rendered.
- (8) Prizes for advertising purposes or prizes received by racehorse owners.

Among these items, fees or other remunerations paid by individuals not required to withhold income tax on salaries paid to housekeepers are not subject to withholding tax.

b. The following items are subject to a 10% withholding income tax after deductions of the amounts enumerated below:

- (1) Fees or other remunerations to judicial scriveners, land and house inspectors, or marine agents—¥10,000 per payment
- (2) Payment to physicians or dentists for socially insured medical or dental treatment—¥200,000 per month
- (3) Remunerations paid to professional boxers—¥50,000 per payment
- (4) Fees or other remunerations to salespeople or bill collectors—¥120,000 per month
- (5) Fees or other remunerations to bar hostesses—¥5,000 per day
- (6) Prizes for advertising purposes—¥500,000 per payment
- (7) Prizes received by racehorse owners—20% of the prize plus ¥600,000 per

* If certain conditions of the recipient's reliability regarding this tax payment are met and a certificate is obtained from the Tax Office concerned, withholding is not required.

payment

8. Quasi-Financial Products

Interest, profits, and premiums accrued from quasi-financial products such as installment savings, saving accounts offered by mutual loans and savings banks, mortgage securities, gold deposit accounts, lump-sum endowment insurance, or lump-sum casualty insurance are subject to a 15% withholding tax.

9. Others

The following additional items are also subject, upon payment, to withholding tax at the rates given below:

- a. Annual life insurance contract pension payments which, after deducting the amount allocable to paid-in premiums, are in excess of
¥250,000 10%
- b. Distribution of profits from anonymous association contracts etc.20%

2/9 Inquiries and Examinations for Taxpayers and Information Returns

1. Inquiries and Examinations

In the course of examining a taxpayer's income, tax officials may question third parties having transactions with the taxpayer under investigation.

The inquiry may be conducted, at the discretion of the tax official, to the examination of the third party's books and records involving transactions with the taxpayer under investigation.

If the taxpayer or third party declines to answer, gives false answers, refuses inspection, or produces false documents, they may be penalized.

Tax officials may ask for the cooperation of other government agencies (including local government and government-affiliated agencies), including the perusal of documents, the submission of information etc., as is deemed necessary during the examination of the taxpayer's income.

2. Payment Records

For the purpose of securing a correct assessment of income, payers of dividends, interest, salaries, etc., are required under the Income Tax Law to submit the payment or withholding records listed below to the Director of the Tax Office.

These documents are then sent to the Tax Office that has jurisdiction over the residence of the recipient of such income, and Tax Office verifies whether the income has been correctly reported on the return. Penalties apply if payers fail to

submit these or submit false documents.

a. Payment Records for Interest

Under the Income Tax Law, those paying interest (including the payers' agents in charge of payment within Japan) on bank deposits and distributed profits from joint operation trusts and open-end bond investment trusts are required to submit payment records to the Director of the Tax Office by 31 January of the year following the payment if the amount of the annual payment is over ¥30,000 or more.

The Special Taxation Measures Law, however, allows special treatment of payment records for interest income (interest or distributed profits of a specified trust) as follows:

- (1) Regarding interest income paid to a resident or nonresident who has a permanent establishment, a payer (including the payer's agents) need submit no payment record.
- (2) Regarding interest income paid to a domestic corporation, or a foreign corporation which has a permanent establishment, payers may prepare and submit a payment record for each payment to a given person instead of aggregating all payments to that person in the year concerned. In addition, if a given payment is no more than ¥10,000 (¥5,000 if the attributable period of calculation is from six months to less than one year and ¥2,500 if the period is less than six months), a payer need not submit a payment record.

b. Payment Records for Dividends

Under the Income Tax Law, payers of dividends must submit payment records to the Director of the Tax Office within one month from the date of determination of payment (for dividends on shares of stocks of a bearer type or the distribution of gains on uninscribed beneficiary certificates of securities investment trusts from the date of payment) stating the payee's name and address, the amount of payments, etc., if the amount of payment exceeds ¥15,000 (¥30,000 if the period on which the amount of dividend etc. is calculated is over one year).

Under the Special Taxation Measures, however, records are not required on dividends payable provided that the amount of payment per stockholder per day does not exceed the amount which derived by dividing ¥100,000 by the dividend calculation period.

c. Notice of Receipt

A person who receives ① dividends or interest on bearer securities, or ② dividends or interest on a basic deposit or shares of stock should submit his or

her name and address to the person in charge of the payment of such income.

If interest is withheld at the source, however, notice of one's name and address is not required under the Special Taxation Measures Law.

d. Records for Withholding

Payers of employment income or retirement income must prepare records of withholding in duplicate stating the payee's name, address, and amount of payment and tax withheld at the source while submitting one copy to the Director of the Tax Office and the other copy to the payee by 31 January of the following year. Submission of these records to the Tax Office is not necessary if the payment of employment income is under ¥5 million per annum or if the retirement income is to persons other than directors of a corporation. Payees should attach a copy of this withholding record to their tax returns when they conduct final returns.

e. Payment Records for Remunerations, Fees, etc.

Payers of fees or other remunerations, or of the Payment Fund for Medical Treatment Fees that is part of the social insurance system must submit payment records to the Director of the Tax Office by 31 January of the following year stating the payee's name, address, and the amount of payment, etc., if the payment exceeds a certain amount.

CHAPTER III

CORPORATION TAX (CORPORATE INCOME TAX)

3/1 General

1. Characteristics of the Japanese Corporation Tax

- a.** Under the Corporation Tax Law, corporate income tax is levied on the taxable income of corporations. The Special Taxation Measures Law provides certain special measures for specific policy objectives.
- b.** Corporations for tax purposes include not only those corporations in an ordinary sense, but also all types of juridical persons under various names such as cooperatives, public corporations, social welfare juridical persons, labor unions, and so forth. Organizations without juridical personality, such as unincorporated clubs or associations, are regarded as juridical persons for tax purposes so long as they designated representatives or managers. Local public entities, government agencies, public corporations, and other bodies set forth in Table 1 of the Corporation Tax Law are not obliged to pay the corporation tax.
- c.** Corporation tax is levied on the income of each accounting period*, income in liquidation, or in case of trust and insurance companies, Japan Mutual Aid Agricultural Co-operation (Zen-Kyo-Ren), etc., dealing with the Welfare Pension Fund Plan, defined benefit pension plan asset management contracts, etc., the remaining balance of the retirement pension surplus reserve at the beginning of each accounting period. In the case of a family corporation, an additional tax is levied on the retained profits for each accounting period when these profits exceed a certain prescribed level.

Unlike the individual income tax, no preferential treatment is allowed for capital gains in computing taxable corporate income. Sales of the land are treated specially according to the holding period stipulated in The Special Taxation Measures Law. (This rule is not applied from January 1, 1998 to December 31, 2008)

- d.** Since the overall reform of the taxation system in 1950 that followed the Shoup Recommendations, the corporation tax system has been in principle based on the notion that a corporation is an aggregate of shareholders and that there should be an integration of tax burdens, though the method of

* In Principle, taxable income is calculated according to the GAAP (Generally Accepted Accounting Principle)

mitigating tax burdens has changed somewhat over the years.

In the early years, the alleviation of tax burdens was done wholly at the shareholder level. The corporation's taxable income was taxed at 35% whether it was distributed or not. The dividends received by an individual shareholder were included in his taxable income together with income from other sources. (However, the amount equivalent to 25% of the dividends received could be credited towards his or her income tax, 25% being the approximation designed to make the overall tax burden on dividends (i.e., the corporation tax paid at the corporation level plus income tax) around 60% for an individual in the highest bracket of the income tax rate schedule.) Dividends received by a corporation were not included in the taxable income for a corporation due to tax purposes.

In 1961, a split-rate system was introduced in order to increase the equity capital of the corporation vis-à-vis borrowed capital. The underlying philosophy of the tax reform was to implement the mitigation partly at the company level and partly at the shareholder level. The tax rate on distributed profits was reduced from 38% to 28%, while the tax on undistributed profits remained at 38%. Correspondingly, the dividend credit with respect to income tax was reduced from 20% to 15% of the dividends received. It was subsequently stipulated that in cases where the dividends received by a corporation exceeded those distributed, a quarter of the balance should be included in the taxable income of the corporation.

There have been some changes in tax rates since that point, but the basic structure of corporate taxation system remains unchanged.

In recent years, there have been various arguments about the corporate taxation system. In the tax reforms of 1989, the reduced tax rate on distributed profits (which was 32% while the tax rate on retained profits was 42%) was abolished and a rate of 37.5% was applied to both retained and distributed profits from 1 April 1990. The present tax rate is 30%, applied after 1 April 1999.

- e. For corporations with capital of no more than ¥100 million, reduced tax rates are applicable for income of no more than ¥8 million. The tax rate became 22% after 1 April 1999. In addition, for public service corporations, etc. in Schedule 2 and cooperatives, etc. in Schedule 3 of the Corporation Tax Law, a reduced rate of 22% is applied.
- f. The amount of tax on the interest, dividends, and redemption premium of discount securities withheld at the source can be credited to the amount of the corporation tax paid in the current year. If the amount of tax withheld at III Corporation Tax (Corporate Income Tax) the source exceeds the amount of corporation tax, the excess amount will be refunded.

Corporation Tax (Corporate Income Tax)

- g.** Corporation tax is paid under the self-assessment system. A corporation must file a corporation tax return, together with a balance sheet and a statement of profit and loss, to the Director of the Tax Office, in principle, within two months of the end of each accounting period, and must pay the tax as reported on the return. If taxpayers fail to file correct returns, tax authorities reassess returns through a procedure of correction or determination.
- h.** Local inhabitants tax and enterprise tax are levied by local authorities on corporations based on corporate income etc.

In the tax reform of 2001, measures on taxation on corporate reorganization had been taken. In the tax reform of 2002, a consolidated taxation system was introduced. For the outline of the corporate reorganization taxation, see P. 80 and after. For the outline of the consolidated taxation system, see P. 82 and after.

2. Special Taxation Measures

The Special Taxation Measures Law provides various measures designed to help attain certain economic policy objectives, such as energy conservation, pollution control, regional development, and promotion of small and medium-sized enterprises. These measures range from deduction measures, such as a tax credit and income deduction, to tax deferral, such as special depreciation and advanced depreciation. The loss of the revenue are estimated to ¥ 1,088 (billion yen) (See the table on page 86). These special taxation measures are provisional and the application periods are stipulated in the law. The Special Taxation Measures are taken on an exemption of the principle of taxation, “equity, neutrality, and simplicity,” from a viewpoint of realizing specific policy purposes, and it is necessary to promote consolidation and rationalization by always examining adequately their policy purposes, effects, and appropriateness as policy means.

Tax Measures Concerning Corporate Reorganization Including Corporate Division, Consolidation, etc. <Outline>

1. Taxation on Corporations

- When assets are transferred, capital gains on transfer of assets will be taxed in principle. However, in the following cases of corporate reorganization, taxation will be deferred. (In the case where monetary consideration is provided, taxation on capital gains will be applied according to the principle.)

Classification	Requirements
<div style="border: 1px solid black; padding: 5px; margin-bottom: 10px;">Reorganization within a corporate group</div> <p>(Equity share: more than 50%)</p>	1) Transfer of an independent business unit (Major assets and liabilities + Considerable number of its employees) 2) Continuation of the transferred business * If the equity share is 100%, the requirements of the above 1) and 2) are not necessary.
<div style="border: 1px solid black; padding: 5px; margin-bottom: 10px;">Reorganization to form a joint venture</div> <ul style="list-style-type: none"> ○ The businesses must be related to each other, and ○ The scale of the businesses is not substantially different. <div style="display: flex; align-items: center; margin: 10px 0;"> <div style="font-size: 2em; margin-right: 10px;">{</div> <div style="text-align: center;"> The difference in the ratio of sales, number of employees, or other similar conditions is no greater than approximately 1:5 </div> </div> <ul style="list-style-type: none"> or ○ Participation of managing directors and upper level directors in management 	1) Transfer of an independent business unit (Major assets and liabilities + Considerable number of its employees) 2) Continuation of the transferred business 3) Continuation of holding of the shares acquired in consideration of the assets transferred

2. Taxation on Shareholders

- When only the shares in the successor company, etc., after division are delivered to shareholders, taxation on capital gains or losses on old shares will be deferred.

3. Handling of Reserves, etc.

- Regarding succession of reserves, the required measures will be taken in accordance with the form of corporate reorganization.

4. Preventive Measures against Tax Avoidance

- In addition to the prevention regulation of tax avoidance using losses carried forward, etc., prepare a comprehensive tax avoidance prevention regulation regarding corporate reorganization.

5. Others

- Implement tax relief measures, such as reduction of the registration license tax for commercial registration and real property registration accompanied by corporate division, to the same level as consolidation.

Transfer of assets by corporate division, as in the case of consolidation, does not fall under transfer of assets in terms of the consumption tax.

(Note) Applied to corporate reorganizations carried out after April 1, 2001.

Outline of Consolidated Tax Payment System

(1) Object of Application

- A parent company and all of its subsidiaries (excluding foreign corporations) whose stocks are directly or indirectly possessed by the parent company on a 100% basis
- Only an ordinary corporation or a cooperative association can be a parent company, while only an ordinary corporation can be a subsidiary.
- The stocks of the employees, holding group and certain stocks acquired with a stock option shall be excluded from determination of possession rates.
- Application of the consolidated taxation system may be selected subject to obtaining an approval from the Commissioner of the National Tax Agency. However, the consolidated taxation system once selected shall be continuously applied.
- A corporation having left the consolidated group shall not be allowed to rejoin the group for five years thereafter.
 - 1) Consolidated Group 2) Domestic 3) Parent Company
 - 4) Overseas 5) Affiliate Company 6) Subsidiary
 - 7) Sub-subsidiary Company

(2) Declaration and Payment

- The parent company shall declare and pay the corporation tax.
- Subsidiaries are responsible for payment of the consolidated tax and shall submit the relevant individual amounts to the taxation office.
- The consolidated business year shall conform to the business year of the parent company.

(3) Calculation of incomes and tax amounts

- The amount of the consolidated income obtained by adjusting the incomes of individual corporations shall be multiplied by the tax rate. Further adjustment shall be made to calculate the consolidated tax amount.
- The tax rate shall be the same as the current tax rate in principle.
 - ① In case the parent company is an ordinary corporation: 30%
 - ② The reduced tax rate in case the parent company is a small or medium-sized corporation (the part of ¥8 million or less to be covered p.a.): 22%
 - ③ The reduced tax rate in case the parent company is a cooperative association: 23%
- The consolidated loss shall be subject to a deferred deduction for seven

years. Losses of the parent company and the complete subsidiary related to stock transfer before consolidation shall be subject to deferred deduction as a consolidated loss.

- In transfer of the stocks of a subsidiary, to prevent double calculation of profits and losses, the booked value of the subsidiary's stocks shall be modified at the time of transfer.

(4) Handling of various systems

- Concerning various systems as provided in Corporation Tax Law and Special Taxation Measures Law, the consolidated group shall be basically handled as a unity, and regulations shall be prepared based on the purposes of the individual systems.
- No loss interest shall be deducted from dividends received from corporations belonging to the consolidated group and the dividends as a whole shall not be added to profits.
- The cost of depreciation shall be separately calculated by the individual corporations.
- The amount of donations not added to the losses shall be calculated for the consolidated group as a unity based on the amounts of consolidated incomes and the capital of the parent company. No amount of contributions to and from the corporations belonging to the consolidated group should be added to the loss.
- Deduction for doubtful accounts shall be separately calculated by the individual corporations after removing money claims among the corporations belonging to the consolidated group.
- The amount of disallowable expenses such as entertainment expenses not qualified for deduction shall be calculated for the consolidated group as a unity based on the capital of the parent company.
- Income tax deduction shall be applied to the consolidated group as a unity.
- Limits to deduction of foreign taxes shall be calculated for the consolidated group as a unity. The total amount after adjustment made for each corporation shall be deducted.
- In case the parent company is a family corporation, its retention money shall be taxed on the consolidated group as a unity.
- The tax deduction for the costs of research shall be applicable to the consolidated group as a unity.
- The tax deduction for investment in plant and equipment shall be calculated for the individual corporations and shall be limited to a certain

amount of the consolidated tax amount.

(5) Handling of transactions made within the consolidated group

Capital losses from asset transactions made among the corporations belonging to the consolidated group shall be calculated by the corporation which acquires the relevant asset at the time of the transfer.

(Applicable to fixed assets, land, negotiable securities, money claims or deferred assets whose book values are ¥10 million or more)

(6) Valuations at the current price of the assets at the time of commencing the application and joining the group

○ In commencing the application or joining the consolidated taxation, profits or losses shall be valued at the current price of the assets of the corporation concerned.

(Applicable to fixed assets, land, negotiable securities, money claims or deferred assets whose latent profit or loss is half of the capital amount or ¥10 million, whichever is the smaller)

○ The parent company, complete subsidiaries concerned with stock transfer, or a subsidiary owned for a long time (more than five years) or subsidiaries arising from a qualified merger or through a certain stock exchange shall not be applicable.

(7) Others

○ Regulations have been established for prevention of comprehensive tax avoidance.

○ Regulations have been prepared concerning inquiry and inspection rights or punishment.

(8) Measures for Financial Resources

○ The measures are applicable within the framework of the consolidated taxation system

① Consolidated additional tax (2%) for 2years (abolished from April 1, 2004)

② Restriction on carrying-in of losses of the consolidated subsidiary arising before consolidation

③ Restriction on joining of new subsidiaries

○ Review of Taxation Base

① Review of the system where received dividends are not added to the profit (reduction in the ratio from 80% to 50% of the stocks other than

those of the consolidated corporation or affiliated corporations not to be added to the profits) (Interim measure is allowed for small and medium-sized corporations).

- ② The system to reserve for retirement deductions shall be abolished and disposed of in four years (ten years for small and medium-sized corporations)
- ③ The former system to reserve for special repairs with an interim measure allowed shall be abolished and disposed of in four years.

**Trial Calculation of Loss in Revenue as an Effect of Special
Taxation Measures for Corporation**

(FY 2005 revenue estimates, In billion yen)

A. Special Depreciation		
1. Special depreciation on specified equipment, etc.		
(1) Anti-pollution equipment	△	4.0
(2) Sea craft	△	1.0
2. Special depreciation on medical equipment, etc.	△	8.0
3. Immediate write-offs for depreciation of low-value assets	△	40.0
4. Others	△	15.0
Sub-total	△	68.0
B. Reserves		
5. Reserve for the removal and disposal of Nuclear material used in power generation	△	16.0
6. Reserve for unusual danger	△	19.0
7. Others	△	20.0
Sub-total	△	55.0
C. Tax Credits and income deduction, etc.		
8. Credit in case of conducting research and development	△	597.0
9. Taxation measures to promote the reform of the structure of energy supply and demand	△	28.0
10. Credit for promoting investment by small and medium sized enterprises	△	211.0
11. Taxation measures to improve management fundamentals of small and medium-sized enterprises	△	3.0
12. Taxation measures to improve management fundamentals on Information	△	100.0
13. Tax credit in case of increase in human investment.	△	14.0
14. Others	△	12.0
Sub-total	△	965.0
Total Revenue Loss	△	1,088.0

3/2 Taxpayers

1. Scope of Taxpayers

a. Taxable Corporation

Corporation tax is levied on both domestic and foreign corporations. This chapter, however, deals mainly with the taxation of domestic corporations. For taxation of foreign corporations, see **24/2**.

The corporation tax is levied not only on corporations in the ordinary sense, but also all other juridical persons and certain organizations not considered a juridical person.

According to the Corporation Tax Law, corporations are grouped under the following four headings:

- (1) Ordinary corporations (a joint stock company, Gōshigaish, Gōmeigaisha, other companies, etc.)*
- (2) Public corporations (such as local public entities, etc. listed in Schedule 1 of the Corporation Tax Law)
- (3) Corporation in the public interest, etc. (such as foundations and corporate juridical persons listed in Schedule 2 of the Corporation Tax Law)

* The types of juridical persons treated as ordinary corporations for corporation tax purposes are illustrated below:

Name of ordinary corporations	Created under:
1. <i>Kabushikigaisha</i> (joint stock company)	Corporate Code
2. <i>Gōshigaisha</i>	Corporate Code
3. <i>Gōmeigaisha</i>	Corporate Code
4. Japanese version LLC (Godo-Kaisha)	Limited Company Law
5. Mutual insurance company	Insurance Business Law
6. Joint enterprise cooperative	Small Enterprise, etc., Cooperative Law
7. Medical corporation	Medical Law
8. Intermediate corporation	Intermediate Corporation Law
9. Fishermen's production association	(only those paying remuneration to their own working members) Aquatic Cooperative Association Law Forest Law Agricultural Cooperative Association Law
10. Forestry production association	
11. Agricultural affairs corporation	

(4) Cooperatives (such as agricultural cooperative associations and cooperatives of small-to-medium-sized corporations listed in Schedule 3 of the Corporation Tax Law)*

(5) Non-juridical corporations with designated representatives or managers
Public service corporations are subject to corporation tax only on the

* Juridical persons falling under the category of cooperative association are as follows:

Name of cooperative associations	Created under:
1. Living Sanitation business associations and related federations (excluding those without capital) and living sanitation small business associations	Law concerning the Proper Operation promotion of Living Sanitation Business
2. Federations of fishery cooperative associations, fishing cooperative associations and related federations, fishing product associations	Fishery Cooperative Association Law
3. Commercial and industrial associations (excluding those without capital)	Law concerning the Organization of Small Enterprise Associations
4. Central Cooperative Bank for Commercial and Industrial Associations	Central Cooperative Bank for Commercial and Industrial Associations Law
5. Federations of commercial and industrial associations (excluding those without capital)	Law concerning the Organization of Small Enterprise Associations
6. Shopping center promotion associations and related federations	Shopping Center Promotion Association Law
7. Consumers' cooperative associations and related federations	Consumers' Cooperative Association Law
8. Shinkin banks and related federations	Shinkin Bank Law
9. Forestry cooperative associations and related federations	Forestry Association Law
10. Aquatic products processing cooperative associations and related federations	Fishery Cooperative Association Law
11. Forestry production cooperative associations (excluding those paying remuneration to their own working members)	Forestry Association Law
12. Shipowners' mutual insurance associations	Shipowners' Mutual Insurance Association Law
13. Tobacco cultivation associations	Tobacco Cultivation Association Law
14. Small enterprises etc., cooperative associations (excluding joint enterprise cooperatives)	Small Enterprise, etc., Cooperative Association Law
15. Inland waterways transport associations and related federations	Inland Waterways Transport Association Law
16. Agricultural cooperative associations and related federations, and agricultural affairs corporation (excluding those designated by the Minister of Finance)	Agricultural Cooperative Association Law
17. Central Cooperative Bank for Agriculture and Forestry	Central Cooperative Bank for Agriculture and Forestry Law
18. Export associations (excluding those without capital)	Export and Import transaction Law
19. Export fishery associations	Law concerning the Promotion of Export Association
20. Import associations (excluding those without capital)	Export and Import transaction Law
21. Labour credit associations and related federations	Labor Credit Association Law

Corporation Tax (Corporate Income Tax)

income derived from business defined as a profit-making activity. For income derived from assets not pertaining to “profit-making activities,” neither income tax nor corporation tax is levied in principle.

A non-juridical organization which has either a designated representative or a manager is treated as a corporation for corporation tax and income tax purposes, and only the income derived from “profit-making activities” is taxable.

b. Nontaxable Corporation

Among the organizations not imposed corporation tax are the Government of Japan, its agencies, and local public entities such as prefectures, municipalities etc., corporations established by contributions from the government and/or local public entities, such as the Housing Loan Corporation and the National Students’ Aid Fund, and other organizations listed in Schedule 1 of the Corporation Tax Law.

2. Rules for Income Attribution

a. Principle of Attribution of Income to an Actual Beneficiary

The principle of attribution of income to an actual beneficiary applies for corporation tax purposes in the same way as for individual income tax purposes (see 2/2, 2).

For example, if shares of a corporation are nominally held by its executives, and if the de facto rights thereto remain with the corporation, the dividends and profits from sales of such shares are deemed to be attributable to the corporation.

b. Taxation of a Trust

If a beneficiary of a trust is specified, corporation tax is levied on earnings from property in trust as if the beneficiary owns such property (or, in the case that the beneficiary is not specified, as if the grantor owns such property). However, revenue and expenses of trust companies on the property held under joint operation trusts, investment trusts, trusts for approved retirement pensions, trusts for welfare pension funds, trusts for national pension funds, and trusts for the Employees’ Assets Formation Plan etc. are not included in the revenue or expenses of the trust companies. Earnings of trusts duly distributed are treated as the beneficiaries’ income and the taxable income of the trust company consists only of the amount received as trust fees.

3/3 Taxable Income

1. Principle of Calculation of Taxable Income

As mentioned earlier, corporation tax is levied on the net income for each accounting period, on the net income in liquidation, or on the remaining balance of retirement pension funds. The taxable income is calculated on the basis of books and records which the Commercial Code and other laws and regulations require each corporation to keep.

The taxable income of the corporation for each accounting period is the excess of gross revenue over the total of its costs and business expenses. Gross revenue is the increase in the value of assets accruing from every transaction of the corporation exclusive of gains from certain capital transactions such as premiums or paid-in surpluses of stocks, gains from stock retirement, or a portion of gains from reduction of capital in a merger, etc. Broadly, “business expenses” are the decrease in the value of net assets from all causes other than reimbursement of capital or distribution of profits.

In short, gross revenue minus expenses represents the corporate net income for tax purposes. Though the tax laws require or allow some adjustments in corporate profit calculated in accordance with generally accepted accounting principles in arriving at taxable income, the calculation of corporate net income generally follows the normal practices of modern accounting principles. Corporate net income for tax purposes thus coincides with corporate profit before taxes as shown in the profit and loss statement for the corporation.

When a corporation ceases to exist, either by dissolution or by merger, corporation tax is charged on its liquidation income at the time of such dissolution or merger.

2. Items Excluded from Gross Revenue or Gross Expenses in Calculation of Taxable Income

a. Items to be Excluded from Revenue for Tax Purposes :

- (1) 50% (in the case of specific shares*, 100%) of dividends less a portion of the interest paid by the corporation on borrowed funds.
- (2) Profit from the appreciation of assets.
- (3) Refunds of corporation tax, prefectural inhabitants tax and municipal inhabitants tax.

* Specific shares are ones which are possessed in excess of 25% of the portion of all published shares.

b. Items to be Excluded from Expenses for Tax Purposes

- (1) Write down of assets. However, a write down to the market price is allowed as a financial loss in the event of (a) an inventory with excessive wear and tear, (b) a remarkable decline of listed stock prices or (c) excessive damage of fixed assets due to disaster. When the firm is under such a special occasion as control under the Civil Revitalization Act, some portion of their write down assets are allowed as financial Tax deductible loss.
- (2) Capital expenditures that lengthen the useful lives of fixed assets or increase their value.
- (3) (a) Directors' remuneration other than periodic equal payments, previously registered fixed payments and certain variable payments connected to profit (exclusive of retirement allowances)
(b) Directors' remuneration exceeding a reasonable level and directors' remuneration paid which is based on disguised facts (including retirement allowances)
(c) The portion of the payments to the chief executive director of certain family corporations, which is corresponding to the employment income deduction (exclusive of retirement allowances)
- (4) Certain amounts of contributions. There are various kinds of expenditures called contributions. Some may be deductible as expenses on the basis of generally accepted accounting principles and others may not. Hence, it is stipulated that a corporation may deduct as expenses part of its contributions up to the amount equal to half of the sum of 2.5% of its income and 0.25% of the terminal capital in the case of ordinary corporations. (The ceiling differs to some extent for other corporations.)

However, there are three exceptions to this rule:

- (a) Contributions to the national or local government: all contributions are deductible.
- (b) Contributions specially designated by the Minister of Finance to public institutions: all contributions are deductible. The Minister of Finance is authorized to designate these institutions under the Corporation Tax Law when they satisfy certain criteria set forth by the Law.
- (c) Contributions to special public-interest-promoting corporations and certain non-profit corporations: contributions to these corporations that are related to the main business of the corporation entitle a corporation to a deduction of the additional amount equal to the amount described above (i.e., half of the sum of 2.5% of the income and 0.25% of the terminal capital). The Corporation Tax Law stipulates that such organizations should be those that make a remarkable contribution to the promotion of

art, education, or science, to the improvement of culture or social welfare, or to the advancement of the public interest.

- (5) Corporation tax, prefectural inhabitants tax, municipal inhabitants tax, additional tax, delinquent tax, penalties, fines, forfeits, and levies by the Emergency Measures Law for Ensuring Stabilization of People's Lives or the Act concerning Prohibition of Private Monopoly and Maintenance of Fair Trade.
- (6) In addition to expenses, which are based on disguised facts and paid out to decrease corporate tax liability, penalties and surtaxes.
- (7) Expenses not supported by vouchers are usually excluded from deductible expenses. Such expenses may not only be nondeductible for the corporation but may also be included in the taxable income of the other party through whom such disbursements are made.

In addition, the amount of social and entertainment expenses exceeding a certain amount* is not deductible for tax purposes. Social and entertainment expenses include social expenses and similar expenses disbursed by a corporation for the purpose of receptions, entertainment, consolation, gifts, and the like related to the business. Expenses disbursed by a corporation to promote the welfare of employees are basically not included.

3. Valuation of Inventories

a. Selection of the Method of Valuation

The eligible methods of inventory valuation for tax purposes, stipulated by the Cabinet Order implementing the Corporation Tax Law, are a cost basis and the lesser of the cost or the market price basis.

Using the cost basis, one of the following methods may be selected by a taxpayer actual cost method, first-in-first-out method, last-in-first-out method, weighted average method, moving average method, straight average method, most recent purchase method, or retail method.

b. Report of Valuation Method

A newly established corporation or a corporation that has changed its business must report to the Director of the Tax Office the method of inventory valuation it has chosen by the time its final corporation tax return for the first taxable year is due. When the corporation fails to report, inventories are valued by the "most recent purchase" method. The special method of inventory valuation reported by the corporation may be upheld if the Director

* For corporations with capital of up to ¥50 million, 80% of the amount of social and entertainment expenses paid on and under ¥4 million are deductible.

of the Tax Office determines that the method will not distort the calculation of corporate income. If a corporation wishes to change its method of inventory valuation, it must obtain the approval of the Director of the Tax Office.

c. Acquisition Cost of Inventories

The acquisition cost of inventories is the purchase price in the case of assets bought from others, the market price in the case of assets acquired as a gift, and the total cost of materials, labor, and all related expenses in the case of assets produced by the corporation itself.

Those acquisition costs include transportation and stevedore service costs, transportation premiums, purchase commissions, customs duties, and all other expenses directly incurred in making inventories available for acquisition or sale.

4. Depreciation Allowance

a. Calculation of Depreciation Allowance

With respect to tangible fixed assets such as machinery, equipment, or buildings (excluding land), intangible fixed assets such as copyrights, patents, business rights, deferred assets, intangible fixed assets (such as experimental research expenses and organizational expenses), or other properties such as cattle and fruit trees, depreciation expenses are calculated on the basis of the acquisition cost, salvage value (10% of the acquisition cost in the case of tangible assets and nil in the case of intangible assets), and the number of years during which such assets are serviceable. The amount depreciable should be calculated using an approved method.

It is stipulated by Cabinet Order, however, that a corporation may deduct the full amount of the acquisition cost of depreciation assets with a useful life of less than one year or acquisition costs of less than ¥100,000 as expenses in the accounting period concerned. It is also stipulated by Cabinet Order that a corporation may deduct all or a part of the acquisition cost of assets less than ¥200,000 for 3 years, dividing the cost into equal amounts for each year. It is stipulated in the Special Taxation Measures Law, that a small or medium-sized enterprise can deduct the acquiring costs of small assets up to ¥3,000,000, each acquiring cost of which is less than ¥300,000. (This measure is effective until March 31, 2008.)

b. Methods for Calculating Depreciation (excluding deferred assets)

Ordinarily, a corporation may elect to use one of the two following methods of depreciation prescribed by the Cabinet Order implementing the

Corporation Tax Law (Only the straight-line method can be used for buildings acquired after 1 April 1998):

- (1) Straight-line method
- (2) Declining balance method

The corporation may elect to use the method for each item or group of properties. Where a corporation has more than one establishment or vessel, it may use a different method of depreciation for each.

In the case of intangible fixed assets, cattle or fruit trees, only the straight-line method can be used.

The unit-of-production method may be selected for depreciation assets for mining use and the replacement method may be selected for specially designated assets to be frequently replaced such as ties and electrical poles. Goodwill acquired before March 31, 1998 may be optionally depreciated.

c. Report on Depreciation Methods (excluding deferred assets)

A newly established corporation must report to the Director of the Tax Office the method of depreciations elected by the time its corporation tax return (the final return) for the first taxable year is due (excluding buildings acquired after 1 April 1998).

If the corporation fails to report, the depreciation should be based on the declining balance method (excluding the depreciation assets for mining use and the mining right, for which depreciation must be based on the production method).

d. Statutory Useful Life and its Adjustment Measure

The useful life of fixed assets for calculating the charge of depreciation is prescribed by statute. The statutory useful life of selected assets is shown in the table on the next page.

The statutory useful life of assets has been determined based on the assumption that the assets are new at the time of acquisition and are used in a normal way. In certain cases, measures allow the adjustment of this statutory useful life to correspond to the actual status of assets. Some examples are:

- (1) Shortening of the useful life

If the asset acquired by a corporation cannot live out the whole of the normal statutory life because of the extraordinary nature of its composition and materials used or condition of the place where it is used, the corporation may submit an application to the Regional Commissioner of the Regional Taxation Bureau for the shortening of the useful life of such an asset.

- (2) Useful life of used assets

Corporation Tax (Corporate Income Tax)

Since a statutory useful life for an asset is not properly applicable to a used asset, a corporation which has acquired such a used asset may rationally shorten its life.

(3) Additional depreciation

In case a corporation operates machinery and equipment used longer than its ordinary time and reports the treatment of them to the Director of the Tax Office, an extra charge for depreciation is allowed.

e. Residual Value (as an Allowable Limit for Depreciation)

As noted earlier, the amount depreciable in one accounting period for tangible assets is calculated on the assumption that the salvage value of the assets will be 10% of the acquisition cost. However, the depreciable amount is 95% of the acquisition cost, which means that a corporation may depreciate, if it so wishes, until the residual value of the asset reaches 5% of the acquisition cost.

The residual value of intangible fixed assets and deferred assets is nil.

f. Treatment of Thin or Excessive Depreciation

The unused portion of depreciation deductions within the limit calculated in the above-mentioned methods may not be carried over.

Depreciation charges in excess of the allowable amount are not deductible as expenses for tax purposes. The balance is carried over to the subsequent accounting period.

Sample of Statutory Useful Lives of depreciation Assets

Description of Assets	Useful Life (years)
(1) Tangible fixed assets other than machinery and equipment	
Reinforced concrete buildings (for offices)	50
Wooden buildings (for offices)	24
Elevators	17
Air conditioners	15
Steel vessels (2,000 tones or larger)	15
Steel tankers (2,000 tones or larger)	13
Steel fishing vessels (500 tones or larger)	12
Airplanes (take off weight of 130 tones or more)	10
Trucks (for transport business)	4
Passenger automobiles (taxis)	4
Computers	4 or 5
Desks, chairs, or cabinets made of metal	15
Typewriters	5
(2) Machinery and equipment	
Chemical constituent manufacturing plants	7
Sugar plants	13
Beer breweries	14
Raw silk manufacturing plants	10
Spinning mills	10
Pulp manufacturing mills	12
Chemical fertilizer manufacturing plants	10
Polyethylene manufacturing plants	8
Synthetic fiber manufacturing plants	7
Rayon yarn or rayon staple manufacturing plants	9
Plate or sheet glass manufacturing plants	14
Cement production plants	13
Steel manufacturing plants	14
Metallic machine tool manufacturing plants	10
Electrical machinery and appliance manufacturing plants	11
Automobile manufacturing plants	10
Lens or other optical instrument manufacturing plants	10
Radio or television broadcasting facilities	6
Hydraulic power generation plants for electric utilities	22
(3) Intangible fixed assets	
Patent rights	8
Utility model rights	5

g. Acquisition Cost of Fixed Assets

The acquisition cost of fixed asset is the purchase price when it is purchased, the total cost of raw materials, labor, and other necessary expenses when it is constructed or manufactured by corporation itself, the market price when it is acquired by the means other than that described above (for instance, gift). Those acquisition costs include transportation and stevedore service costs, transportation insurance premiums, purchase commissions, customs duties, installation costs, and all other expenses directly incurred in making the fixed assets fit for use.

5. Advanced Depreciation

Tax treatment of government grants given to corporations. If a corporation receives a government grant to acquire certain assets and the grant is included in the taxable income, that grant fails to serve its policy objectives substantially. Therefore, the book value of the asset may be reduced by the amount of the grant and the reduced amount may be deducted. This treatment provides a tax deferral.

Examples of similar cases are when:

- ① A fixed asset of a corporation suffers damage and the corporation receives an insurance payment.
- ② A fixed asset of a corporation is exchanged for another certain fixed asset.

6. Tax-Free Reserves

a. Reserve for Bad Debts

The Reserve for bad debts under the tax law is allowed for expected loss in the collection of receivables. The maximum amount deductible as an deduction is the sum of the expected loss of receivables of each category, calculated by the methods shown below:

<i>Categories of receivables</i>	<i>Amount of Expected Loss</i>
Receivables to be valued individually	The amount expected at the end of the accounting period, calculated by a certain method.
Receivables of a category, all items of which are to be valued as a single item	The amount calculated by the empirical rate based on the last 3 years' records of bad debt.

Corporations with capital of no more than 100 million yen are allowed to choose the option of applying certain statutory rates instead of the achieved

provision rate under the Special Tax Measures. As for corporations in the public interest or cooperative associations, etc. the limit to the provision is increased by 16%.

The amount credited to the reserve in each accounting period is added back in full to the income in the following accounting period.

b. Reserve for Loss on Returned Goods

Reserve for losses caused by returned goods may be deducted as losses up to a certain prescribed maximum. This reserve is applicable only to publishers and wholesalers of books and magazines, and manufacturers or wholesalers of pharmaceuticals, agricultural chemicals, cosmetics, ready-made suits, phonograph records, or records for magnetic voice reproducers or the records for voice reproducers of digital system who sell the major part of their merchandise under repurchase covenant, etc. of the major part of their inventory assets.

The amount credited to the reserve in each accounting period is added back in full to the income in the following accounting period.

7. Profit or Loss from the Transfer of Securities and their Term-end Assessment

a. Profit or Loss from the transfer of securities

An amount incurred through the transfer of securities is computed by deducting an amount of costs from the considered amount for the transfer; this is revised upwards in the business year in which the transfer contract went into effect.

In this case, the amount of costs is computed by multiplying per unit on-the-book value, which is calculated based on the moving average method or the weighted average method, by the number of securities transferred.

b. Term-end assessment of securities and their appraised profit and loss

The term-end appraised value of securities for sales is the amount assessed by the market value basis; securities not held for sales are determined on the amount by cost basis.

In addition, for securities not held for sales, the amount of those assessed with the cost basis despite their defined redemption periods and redemption prices equals the amount added or subtracted by an amount to be allocated to each business year out of the difference between the book value and redemption prices.

If securities for sales are held at the end of the business year, appraised

profits or losses on the securities are included either in profit or in loss for the purpose of calculating income for the business year.

c. Profit or loss from derivatives transactions

As for unsettled derivatives that corporations own at the end of the business year, profits or losses due if settled at the end of the business year are included either in profit or in loss.

d. Profit or loss on effecting hedges

If a corporation effects derivative transactions to decrease losses due to the fluctuation in the value of assets or liabilities and the transactions are judged effective in reducing the losses of hedged assets, profits and losses made by the settlement of the derivative transactions, or an amount that corresponds to profits or losses accrued from spared settlements are carried over to the business year in which transactions for the assets of the hedging transactions or the transfer of liabilities took place.

Furthermore, if a corporation effects derivative transactions to reduce expected losses due to fluctuations in the value of securities not held for sales and the transactions are judged effective in reducing losses of the difference between the market value and the book value of the securities, the amount corresponding to profits or losses accrued from the derivative transactions is included either in loss or in profit.

e. Conversion of foreign-denominated transactions

If an internal corporation has a business transaction on a foreign denominated basis, the volume is translated into yen at the exchange rate at the time the transaction took place.

If the yen conversion rate is determined for foreign-denominated assets or foreign-denominated liabilities in a future exchange rate agreement and that result is described in the books when the future exchange rate agreement occurs, the foreign-denominated assets or liabilities are converted at term defined conversion rate for the year.

Incidentally, the term-end conversions of foreign-denominated assets are:

- (1) Foreign-denominated credits and debts the accrual conversion method or the term-end conversion method
- (2) Foreign-denominated securities
 - (a) Securities for sales—the term-end method
 - (b) Securities not held for sales (those with defined redemption periods or redemption prices)—the accrual conversion method or the term-end conversion method.

- (c) Securities not held for sales (other than those described in (b))—the accrual conversion method
- (3) Foreign currency deposit the accrual conversion method or the end-term conversion method
- (4) Foreign currency the term-end method

8. Special Rule for the Recognition of Specific Profits and Expenses

a. Special Accounting Methods Regarding Profits and Expenses of Long Term Installment Sales, etc.

With regard to installment sales of commodities, etc. that satisfy certain requirements, such as those specifying that installment periods are more than two years, profits and expenses may be calculated by the deferred payment method.

Between fiscal year 1998 and fiscal year 2002, with regard to installment sales, etc. that satisfy the requirements of the installment method before abolishment, a certain percentage of profits can be deferred as a transitional rule.

b. Special Accounting Methods Regarding Profits and Expenses of Long-term and Large-scale Construction.

If a long-term and large scale-construction contract (including manufacture) has a construction period of more than two years and a contract price of more than 5 billion yen, profits and expenses in each accounting year are calculated by the percentage of completion method. This provision applies only to construction contracts with a contract price of more than 15 billion yen made between 1 April 1998 and 31 March 2001 and construction contracts with a contract price of more than 10 billion yen made between 1 April 2001 and 31 March 2004.

With regard to construction contracts (excluding construction with an expected loss) except long-term and large-scale construction contracts, profits and expenses in accounting periods may be calculated the completed contract method or by the percentage of completion method.

3/4 Calculation of Tax Amounts

1. Methods of Tax Calculation

a. Corporation Tax on Income for Each Accounting Period

The corporation tax on income for each accounting period is calculated by multiplying the taxable income of the corporation by the tax rates mentioned

Corporation Tax (Corporate Income Tax)

below. Family corporations, as defined later, are subject to an additional special tax on retained earnings exceeding a prescribed level.

b. Corporation Tax on Liquidation Income

The corporation tax on liquidation income is obtained by multiplying amounts by applicable tax rates.

2. Tax Rates

Corporate tax rates from April 1 1999 are shown below.

a. Tax Rates for Ordinary Income

- (1) Ordinary corporations
 - (a) Corporations with capital of more than ¥100 million30%
 - (b) Corporations with capital of no more than ¥100 million
 - For annual income of more than ¥8 million30%
 - For annual income of no more than ¥8 million22%
- (2) Cooperative associations and public service corporations22%

b. Tax Rate for Retirement Pension Funds

1% of the beginning-of-year balance of the retirement pension funds at trust companies, life insurance companies and others which handle retirement pensions

(Taxation suspended until 31 March 2008)

c. Tax Rates for Liquidation Income

- (1) Ordinary corporations 27.1%
- (2) Cooperative associations, etc. 20.5%

d. Reduced Rate Applicable to Special Medical Corporations

.....22%

Reduced rate is applicable to a medical corporation which is approved by the Commissioner of NTA to contribute to the promotion of medicine or social welfare under the condition that the concerned medical corporation is operated properly in the public interest and will not specially contribute to the founder or the person concerned.

3. Tax Credits

a. Income Tax Credits

The income tax withheld on interest, dividends, and redemption premiums, etc., that the corporation has received during the accounting year are

creditable with respect to corporation tax. Such credit is not granted to foreign corporations having no place of business in Japan for income tax withheld on income not subject to corporation tax nor to foreign corporations with a place of business in Japan for income tax withheld on dividends which cannot be attributed to a place of business in Japan (see 24/2).

b. Credit for Foreign Taxes

(1) Introduction

The foreign tax credit system in the Japanese corporate tax legislation can be divided into three systems.

- (a) Direct Credit System: Foreign tax incurred by the taxpayer himself or herself can be offset with respect to Japanese tax, which is calculated using worldwide income as the tax base.
- (b) Indirect Credit System: Under the indirect credit system, out of the foreign tax paid by the first-tier foreign subsidiary (including the foreign tax paid by the second-tier subsidiary that is considered to have been paid by the first-tier subsidiary), an amount corresponding to the dividends received is considered to be paid by the parent company and such underlying foreign tax is allowed to be credited against Japanese taxation of the parent company when it receives dividends. At the same time, the amount of indirect foreign tax credited is added back to the taxable income of the parent company. Thus, through the indirect tax credit system, a foreign subsidiary is treated the same as a foreign branch.
- (c) Tax-Sparing Credit System: Foreign tax credit is also allowed with respect to the amount of foreign tax “spared”, i. e. amount of tax relieved by a foreign country.

Many developing countries have introduced various tax incentives in order to attract investment from abroad. Without the tax-sparing credit system, even if such tax incentives exempt Japanese investors from tax in a foreign country, they are taxed on worldwide income in Japan and the spared amount will only be transferred from the treasury of the developing country to that of Japan through smaller foreign tax credits allowed in Japan. The result is that no tax benefits remain in the hands of the investors. Therefore, the tax-sparing credit system does not annul the effect of tax incentives adopted by developing countries.

(2) Creditable Foreign Taxes

(a) Creditable Foreign Tax

Foreign taxes creditable are taxes that ① are incurred directly by the taxpayer; ② are levied by foreign governments and local authorities in

Corporation Tax (Corporate Income Tax)

accordance with tax laws there; ③ are levied on corporate income and; ④ have the same characteristics as Japanese income tax, corporation tax, and local income-based taxes. Thus, foreign corporate tax on the income of foreign branches and foreign withholding tax on interests/dividends are creditable but foreign taxes that have the characteristics of penalties/royalties may not be credited.

As of business years beginning on and after 1 April 1989 (there is a progressing provision for ②), the following restrictions were introduced with respect to creditable foreign taxes:

- ① The amount of foreign tax corresponding to the amount by which the tax amount exceeds 50% of the tax base in the foreign country is no longer eligible for foreign tax credit, but can only be deducted from income as expenses.
- ② A limit is placed on the eligible amount of foreign withholding tax (including taxes “spared”) that is levied on the gross amount of interest (see the table below).^{*} The rest of the withholding tax (except “spared” tax) will be deducted from income as expenses.

The following taxes, which arise from transactions after April 1, 2001, shall not be included in the foreign tax credit.

- 1) A tax which can be claimed optionally by the taxpayer to refund after the tax has been paid;
- 2) A tax whose payment grace period can be decided by the taxpayer;
- 3) A tax imposed on a capital transaction, including refund of investment;
- 4) Resulting from conference in transfer pricing taxation, a tax imposed as a deemed dividend on the taxable amount a Japanese corporation is reduced by correction
- 5) Foreign corporation tax on income derived from a transaction considered unusual

Classification by Business		Creditable Amount for Individual Withholding Tax
Companies whose main business is the financial business, including securities business		
Average ratio of net taxable income to total revenue in	10% and less	up to 10% of the interest

^{*} Withholding taxes on interest concerning loan arrangements concluded or securities issued prior to the first business year beginning on and after 1 April 1989 will not be subject to the newly introduced restrictions for the first 5 business years from that date. Withholding tax on interest concerning loan arrangements concluded or securities issued in the business years beginning on and after 1 April 1989 will be subject to the new regulations from the outset.

Corporation Tax (Corporate Income Tax)

	the business year concerned and the 2 preceding years (“profitability”)	20% and less	received 15% of the interest
		more than 20%	received full amount
Other companies whose ratio of interest revenue to the sum of interest revenue and gross profit is not less than 20%			
	Average ratio of net taxable income to the sum of gross profit and non-operating revenue in the business year concerned and the 2 preceding years (“profitability”)	10% and less	up to 10% of the interest
		20% and less	received 15% of the interest
		more than 20%	received full amount

(b) Creditable Indirect Foreign Tax

Underlying foreign tax with respect to the dividends received by a Japanese company is creditable as indirect foreign tax.* The creditable foreign tax is computed as follows;

$$\text{Creditable indirect foreign tax} = A \times \frac{\text{Dividends received}}{C - B}$$

A : Foreign tax imposed on the income of the first-tier foreign subsidiary (including the foreign tax imposed on the second-tier subsidiary, which is considered to have been paid by the first-tier subsidiary)

B : Foreign tax imposed on the income of the first-tier foreign subsidiary

C : Income of the first-tier foreign subsidiary**

However, as from business years beginning on and after 1 April 1989, the amount of foreign taxes on dividends eligible for indirect foreign tax credit is limited to the amount calculated by the formula below,** provided that this amount is smaller than the amount computed by the formula above.

* An indirect foreign tax credit is permitted for a domestic corporation with respect to the dividends received from foreign corporations, provided that the domestic corporation owns, for a period no shorter than 6 months before the day when the obligation to pay dividends is confirmed, at least 25% of the shares/voting-shares of that foreign company and its subsidiary.

** The income of the foreign subsidiary used as “C” is the larger of the following :

- (a) Income of the foreign subsidiary on the basis of which dividends to be distributed are computed (income for financial accounting purpose), or
- (b) Income computed according to local tax laws plus (i) corporation tax treated as an expense and local to income exempt from the corporation tax.

*** This formula is obtained by resolving the following in which the sum of the creditable indirect tax and the withholding tax is equal to 50% (effective corporate tax in Japan) of the income subject to Japanese corporate tax, i.e; the sum of the dividend income and the creditable indirect tax.

$$X + E = 50\% \times (X + D)$$

Corporation Tax (Corporate Income Tax)

$$\begin{aligned}\text{Creditable indirect foreign tax (X)} &= \\ &\text{Dividends received (including w/h tax) (D)} \\ &\quad - 2 \times \text{Foreign w/h tax on dividends (E)}\end{aligned}$$

(c) Creditable Tax “Spared”

The scope of the tax incentives that enjoy the benefit of tax-sparing credit must be approved beforehand by Japan in a tax treaty between Japan and the country that provides such tax incentives. Creditable tax “spared” can either be a tax on business profits or a withholding tax on investment income, i.e. dividends, interests, and royalties. It may be credited in the form of either direct tax credit or indirect tax credit.

(3) Credit Limitation

The purpose of allowing tax credit for Japanese corporations is to eliminate double taxation on their foreign source income. It is important to prevent the credit from spilling over into their Japanese source income and reducing the Japanese tax on that income.

Japan achieves this by setting certain limitations on the amount of foreign tax that can actually be credited. Japan adopts “overall limitations” under which all foreign source income and foreign taxes are added to calculate the limitation regardless of the items on which foreign taxes are levied or countries in which taxes are collected. The formula for the limitation is as follows:

Foreign tax credit limitation

$$= \text{Amount of “calculated” Japanese tax} \times \frac{\text{Foreign source income}}{\text{Worldwide income}}$$

Amount of “calculated” Japanese tax

$$= \text{Worldwide income} \times \text{Japanese Corporate tax rate}$$

In calculating the credit limitation, special rules are applied:

- (a) 2/3 of income exempted from taxation in foreign countries* is to be excluded from foreign source income in calculating the credit limitation.
- (b) An upper limit of 90%** is established for the ratio of foreign source income to worldwide income in calculating the credit limitation. With this restriction, Japanese tax corresponding to a minimum of 10% of the total income must be paid in Japan.

(4) Treatment of the Remainder Credit Limitation and the Excess of Foreign Taxes

* Exempted income corresponding to the taxes, “spared,” i.e., deemed to be paid according to tax treaties, shall not be treated as “income exempted from taxation in foreign countries.”

** An exception will be granted to companies that are subject to very severe foreign tax burdens amounting to, as a whole, more than 50% of total worldwide income and to companies with more than 90% of their employees working overseas. For these companies, the ratio of foreign source income to worldwide income may be higher than 90%.

Japan allows taxpayers to carry forward for 3 years the remainder of credit limitations that are not actually used and also to carry forward for 3 years the excess of foreign taxes.

4. Carryover and Carryback of Losses

A corporation consecutively filing a blue return can carry forward losses for seven years following the loss year or carry back losses one year preceding the loss year.

[note 1] For the fiscal years started on and prior to March 31, 2001, deductions can be carried over for up to five years.

[note 2] Except for certain corporations, the above-mentioned carryback provision is not applied to the loss in accounting years ending from April 1 1992 to March 31 2008.

5. Taxation of Retention Money on Family Corporations

This tax is designed primarily to deter shareholders of closely held corporations from attempting to avoid the progressive individual income tax that would be imposed on dividend distributions. Such deterrence is necessary to maintain the equality of tax burdens for corporate and personal enterprises and is accomplished by imposing corporate tax additionally on those corporations' profits retained over a certain level.

A family corporation, which is subject to taxation of retention money, is a corporation more than 50% of whose capital stock is owned by one person, or by individuals or corporations affiliated to that person.

In the case of a family corporation, the retained earnings of an accounting period in excess of the largest of the following three amounts are additionally subject to corporation tax:

- (1) ¥20 million per year
- (2) 40% of the income for the accounting period (50% for corporations whose capital is less than ¥100 million yen)
- (3) The difference between 25% of the paid-in capital and the accumulated surplus (before crediting the retained earnings for the accounting period to the surplus) at the end of the accounting period if the latter is smaller than the former.

This additional tax is calculated at the rates of 10%, 15%, and 20% on brackets of income no more than ¥30 million, over ¥30 million to ¥100 million, and over ¥100 million, respectively.

In determining whether a corporation is additionally subject to a corporation tax on retained earnings, the term "shareholders" excludes corporations that are

Corporation Tax (Corporate Income Tax)

not “family corporations” (more than 50% of stocks of which are owned by one group of shareholder).

6. Special Additional Tax on Retirement Pension Funds of Trust Companies, Life Insurance Companies, etc.

Until the amendment of the Corporation Tax and Income Tax Laws in 1962, the sum which a company transferred to a trust company or life insurance company as a retirement pension fund for its employees was treated as an expense of the corporation but was subject to income tax as employees’ remuneration at the time of transfer. The amendment of 1962 instituted the deferral of the income taxation on employees until the retirement pension becomes payable to the employees and, instead, imposed corporation tax at the rate of 1% per year on the remaining retirement pension funds of trust companies or life insurance companies. This tax is considered interest on income tax during the period of tax deferrals. The welfare pension funds are also subject to this special tax in case its amount is in excess of a certain level. In addition, the accumulated sums of the contribution by a company for its employees based on the Assets Management Plan for Fixed Contributory Pensions, Employees’ Assets Formation Plan, etc. are subject to the tax. However, this taxation is suspended until March 31 2008.

3/5 Returns Payment, and Refunds of Corporation Tax

Like individual income tax, corporation tax is paid under the self-assessment system. A corporation is required to keep simple books of accounts and to maintain records and documents produced or received concerning its business. The corporation income and tax amount must be calculated and a return must be filed by the statutory due date.

1. Final Returns

A corporation’s taxable income and corporation tax due thereon is calculated on the basis of its financial documents as approved by a meeting of shareholders. The return is required to be filed, in principle, within two months after the close of its accounting period. In the event a corporation is unable to, due to a natural disaster, an audit by statutory auditors, or for other inevitable reasons (such as seizure of accounting documents, etc.), have its accounts determined and to file a return by the statutory due date, the tax authorities may grant an extension of the due date.

A final return must be accompanied by the corporation’s balance sheet, profit

and loss statement, and other documents describing items necessary for calculating its income and the corporation tax due thereon.

2. Interim Returns

Corporations with accounting periods exceeding six months are required to file an interim return at the end of the first six months of the period. This results in provisional reporting and prepayment of tax within eight months of the beginning of the period, followed by final reporting and settlement due within two months of the end of the period. This is comparable to the estimated payment of individual income tax.

The corporation tax due on interim returns is usually based on the one due for the preceding period, calculated on a prorated monthly basis. Corporations may elect, however, to calculate the tax on the basis of a provisional settlement of accounts as of the end of the first six months of the accounting period.

No interim return is required if the tax paid or the amount calculated on the basis of the tax payable for the previous accounting period within six months of the end thereof was less than ¥100,000 on a half-year basis.

3. Refunds

The following items pertaining to corporation tax are refundable:

1. Taxes erroneously overpaid
2. The difference of the corporation tax on income arising from the carry back of losses (see **3/6, 2. c**) for the previous year
3. Income tax withheld in excess of the corporation tax due (see **3/4, 3. a**)
4. The amount of foreign tax that is not creditable with respect to the corporation tax for that accounting period but is creditable with respect to the corporation tax for any accounting period in the five preceding years (see **3/4, 3. b**)
5. Excess tax payments in the previous year due to disguised accounting (see **3/7, 2**)
6. The excess of prepaid corporation tax (the difference between the tax prepaid on the basis of the interim return and the tax due on the basis of the final return)
7. The excess of prepaid tax during liquidation (the difference between the tax prepaid during liquidation and the tax due on the basis of the final return)

3/6 Blue Returns

1. The Blue Return System

For the blue return system, reference should be made to the related paragraphs concerning income tax (see 2/7). Primarily due to several privileges under the blue return system, a large number of corporations are filing blue returns.

2. Privileges for Corporations Filing a Blue Return

Privileges granted to corporations filing blue returns are as follows:

- a.** Tax authorities may correct the income of a corporation only when errors are found in the calculation of taxable income based on the corporation's books and pose questions to corporate officers whenever necessary. In making corrections of a tax return, tax authorities must provide the corporation with the reason for such action in writing.
- b.** Losses may be carried over to offset income for the seven succeeding years. Losses generated in the fiscal years started on and prior to March 31, 2001, may be carried over to offset income for the five succeeding years.
- c.** Losses may be carried back to offset the income of the preceding year. In such cases, the tax paid in the previous year that corresponds to the amount of loss carried back is refundable. The application of this measure was suspended from April 1, 1992 until March 31, 2008 except in certain cases.
- d.** Special measures for tax credit (3/8, 1) are granted.
- e.** Special measures for depreciation (3/8, 2) are applicable.
- f.** Various kinds of special taxation measures are applicable.

3. Approval by the Director of the Tax Office

The corporation wishing to file a blue return must present an application to the Director of the Tax Office prior to the beginning of the accounting period for which the blue return is to be filed. The Director of the Tax Office will grant approval to the applicant on the condition that the books of the corporation are kept in accordance with statutory requirements. If necessary, he or she may instruct the corporation as to the proper maintenance of its books.

The Director may revoke such approval if the books are not kept in accordance with the statutory requirements or if there is sufficient evidence to doubt the authenticity of the books. An example is the deliberate omission or false entry of all or part of business transactions. In such cases, cancellation is retroactive to the time when such practices started.

3/7 Correction and Determination

1. Assessment in the Event of Failure to File Correct Returns

Procedures for assessment in the event of failure to file correct returns are the same as in the case of individual income tax (see 2/6, 5).

2. Credit of Corporate Tax Brought by Correction in Case of Overpayment to Disguised Accounting

If a corporation intentionally increases its income by way of disguised accounting and overpays tax accordingly, such an overpayment of tax, upon correction by the tax authorities, cannot be refunded (except that payable in the immediate preceding year) but will be deducted from the corporation tax to be paid in the following five years.

This credit was established to penalize the window dressing of the financial position of a corporation, when a number of cases of manipulating a statement of profits, motivated chiefly by the desire to maintain the level of stock prices or borrowing from a financial institution, occurred and produced severe criticism.

3. Act of Family Corporation etc. and Denial of Calculation

If transactions between family corporations or between family corporations and stockholders thereof result in an improperly low tax liability, the Director of the District Tax Office may disregard such transactions and recompute a corporation's tax liability.

3/8 Special Taxation Measures

1. Special tax credit and income deduction

a. Special Credit for conducting research and development

(1) Tax deduction system for total research expenses:

This system allows a tax deduction equivalent to 8% to 10% of the total test and research expenses depending on their rates (the upper limit is the amount equivalent to 20% of the corporation tax for the relevant period).

The rate of test and research expenses means the rate of test and research expenses against the total amount of sales. (the average sales of four years including the relevant period).

(2) Tax deduction for joint and entrusted researches etc. based on industry-academic-government cooperation:

This system together with (1) allows a tax deduction equivalent to 12% of

Corporation Tax (Corporate Income Tax)

the total test and research expenses for joint and entrusted testing and research with universities and public research institutes (The upper limit is the amount equivalent to 20% of the corporation tax for the relevant period.)

- (3) Tax system to strengthen the technical base of small and medium-sized corporations:

Tax credit of the amount equivalent to 12% is allowed for testing and research expenses instead of applying the above (1) to (2). (The upper limit is the amount equivalent to 20% of the corporation tax for the relevant period.)

Regarding (1) and (3) above, an additional credit for 5% of the amount in excess of the comparable R&D expense is allowed if the R&D expense exceeds the comparable R&D expense and exceeds the standard R&D expense, in the business years starting between April 1, 2006 and March 31, 2008.

With respect to the amount in excess of the upper limit to the tax credit, in case the amount in excess is more than the total test and research expenses for the preceding period, deferment of a year is allowed. (The upper limit to the total of (1) to (3) is the amount equivalent to 20% of the corporation tax for the relevant period.)

- b.** A credit for promoting investment for structural reform of the energy system:

When a corporation acquires equipment for the structural reform of energy supply and demand within the specified period (1992.4.1~2008.3.31), it can elect to receive a special initial depreciation of 30% of basic acquisition costs or a 7% tax credit for up to 20% of the corporation tax liability in the credit year. (Only small and medium-sized enterprises, etc., can elect to use the tax credit.) (The amount excesses upper limit of deduction can be carried over a year.) The portion in excess of the maximum deductible amount can be deferred one year.

- c.** A credit for promoting investment by small or medium-sized enterprises: When small or medium-sized enterprises, etc., acquire specified machines, etc. within the specified period (1998.6.1~2008.3.31), they can elect to use a special initial depreciation of 30% of the standard acquisition cost or a 7% tax credit (up to 20% of the corporation tax liability). Regarding rental assets (except ships), 7% of a certain ratio to total rental fees is allowed as a tax credit. (The amount excesses upper limit of deduction can be carried over a year.) The portion in excess of the maximum deductible amount can be deferred one year.
- d.** A special initial depreciation or a credit for the acquisition of an establishment for improving management fundamentals:

If certain small or medium-sized enterprises, acquire an establishment for improving management fundamentals within specified period (1987.4.1 ~ 2007.4. 1), they can elect to use (1) a special initial depreciation of 30% of the basic acquisition cost or (2) a 7% tax credit (for up to 20% of the corporation tax liability in the credit year). A corporation with capital of more than 30 million yen (Excluding the small and medium-sized businesses stipulated in the Law for the Promotion of New Business by Small and Medium-sized Businesses) cannot use the tax credit. Regarding rental assets, 7% of a certain ratio to total rental fees is allowed as a tax credit. (The amount excesses upper limit of deduction can be carried over a year.)

- e.** Special deduction allowed for corporation tax in the case of acquiring industrial machines in a specified area in Okinawa:

In case a manufacturer acquires industrial machines, etc. within the areas stated below, tax deduction of the amount equivalent to 15% (8% for buildings) of the purchase price is allowed. (The upper limit is the amount equivalent to 20% of the corporation tax for the relevant period.)

- ① Area for promotion of tourism
- ② Area for promotion of information and communication industry
- ③ Area for promotion of advanced industries
- ④ Area for free trade and the special area for free trade
- ⑤ Special area for financial services

- f.** Special depreciation or special deduction for corporation tax in case a specified small to medium-sized entrepreneur in Okinawa acquires facilities for management innovation etc.:

In case a specified small to medium-sized corporation running a business for management innovation based on the Special Measures Law for Promotion of Okinawa acquires facilities for management innovation in accordance with the approved plan to innovate management based on the Law for the Promotion of New Business by Small and Medium-sized Businesses, the corporation may select either 34% special depreciation (20% for buildings) of the price of acquiring the facilities or 15% tax credit (8% for buildings) (The upper limit is the amount equivalent to 20% of the corporation tax for the relevant period.) Also concerning leased assets, a 15% tax credit is allowed for a certain proportion of the total rent. Deferment during four years is allowed for the amount in excess of the limit to the credit.

- g.** Tax system to strengthen information infrastructure:

When a corporation filing blue returns acquires certain equipment to strengthen information infrastructure in the specified period (from April 1, 2006, till March 31, 2008), it is allowed either to consider special depreciation of 50% of the standard acquisition value, or to receive a tax credit of 10% of the

Corporation Tax (Corporate Income Tax)

standard acquisition value (up to the maximum of 20% of the corporation tax liability for the period) .

h. Special tax credit in case investment in human resources increases:

① When the corporations which report the Blue Return invest in human resources and take these expenses as a loss in calculating corporate profit, tax credit, which is equivalent to 25% of the amount of the investment exceeds the comparative human investment (average of the human investment pre-the second term), is allowed (The upper limit is the amount equivalent to 10% of the corporation tax for the same period.). This measure is applied for FY2005 to FY2007.

② When the medium and small-sized business which report the Blue Return invest in human resources and take these expenses as a loss in calculating corporate profit, tax credit, which is equivalent to 50% of the rate of increase in human investment (not more than 20% of the amount of expenses in human resources), is allowed (The upper limit is the amount equivalent to 10% of the corporation tax for the same period.). This measure is applied for FY2005 to FY2007.

i. Special deduction for the incomes of authorized corporations in Okinawa:

In case a corporation authorized in accordance with Special Measures Law for Promotion of Okinawa by March 31, 2007 is newly established in the areas stated below, with its income from special data communication business in the district, an addition to losses in the amount equivalent to 35% is allowed for ten years after its foundation. (For a corporation running a financial business in a special district for financial businesses, deduction of the amount equivalent to 20% of personnel expenses is allowed for the people engaged in such financial businesses.

- ① Special area for information communication businesses
- ② Special area for free trade
- ③ Special area for financial businesses

2. Special Measures for Depreciation

a. In General

(1) In addition to the ordinary depreciation, the following special measures for depreciation have been instituted to attain certain policy aims. Such special depreciation measures, except for specific good houses for rent, are allowed only for corporations filing blue returns, and such corporations may carry over the unused special depreciation deductions to the following year.

Special depreciation deductions may instead be credited to the tax-free special depreciation reserve, and the reserve may equally be added back to

income in the seven succeeding years. (In case the life time of a depreciation asset is less than ten years, the reserve may equally be added back in five years or its life time, whichever is shorter.)

- (2) Special measures for depreciation are broadly grouped into two categories, i.e., increased initial depreciation and additional depreciation.

The increased initial depreciation allows, in addition to the ordinary depreciation, deduction of a portion of the acquisition cost of an asset for the first accounting period in which such an asset is used for business. The additional depreciation permits a corporation to deduct a certain percentage of the ordinary depreciation deduction of an allowable asset for certain consecutive accounting periods, in addition to the ordinary depreciation.

However, it should be noted that neither measure allows the cumulative amount of depreciation to exceed the acquisition cost of the asset concerned. In effect, they provide the benefit of deferred tax payment but not tax exemption.

- (3) As mentioned, the increased initial depreciation allows the extra depreciation in the first accounting period when the assets concerned are used. Additional depreciation is normally given for certain consecutive accounting periods after the first use of the assets. Hence, it is expected that the purchase of such depreciable assets will be encouraged by this measure.

b. Increased Initial Depreciations

- (1) Special initial depreciation on qualifying improved machinery, etc., in the first year of use.
 - (a) Machinery and equipment used for the prevention of environmental pollution……in general, 14% of the acquisition cost. (facilities used for the prevention of environmental pollution: 10%).
 - (b) Steel vessels used to help rationalize the management of international shipping corporations and mitigate the burden of environment: ……16% of the acquisition cost (the rate is 18% in the case of hull tankers for international shipping)
- (2) Special initial depreciation for equipment used in Kansai culture–science research cities for cultural and scientific research ……24% (12% for buildings) of the acquisition cost
- (3) Special initial depreciations for assets used to preserve mountain villages, as specified in the Mountain Villages Promotion Law……13% (6% for buildings)
- (4) Special initial depreciation for assets used in prevention of disasters

Corporation Tax (Corporate Income Tax)

caused by earthquakes

- (a) 8% of assets used in prevention of disasters caused by earthquakes
- (b) 10% of the cost of assets for the prevention of disasters caused by earthquakes and buildings acquired in the course of seismic retrofitting
- (5) Special initial depreciation for industrial machinery acquired and used for certain high-technology business and that is installed designated “technopolises”……14% (7% for buildings).
- (6) Special depreciation of the facilities for business innovation
 - (a) Authorized traders for the plan to introduce the facilities for innovation as provided in Revised Industrial Revitalization Law : 24%
 - (b) Authorized traders for the plan to restructure businesses or the plan to produce businesses for reutilization of management resources as provided in Special Measures Law for Industrial Revitalization : 30%
 - (c) Authorized traders for the plan to restructure joint businesses as provided in Special Measures Law for Industrial Revitalization : 40%
- (7) Special initial depreciation of equipments for digital communication, etc.
 - (a) Equipment enhancing the convenience of telecommunications: 5% of the acquisition cost
 - (b) Equipment to promote dissemination of wide-ranged members network- 10%
 - (c) Convenient equipment used to broadcast……15% of the acquisition cost
- (8) Commercial building, etc. acquired by small or medium-sized retailers…
 - (a) Shared facility or shopping building installed according to maintaining the shopping street program defined in the Law on the Promotion of Small and Medium-Size Retail Business: 8% (12% for the certain shared facilities)
 - (b) Shared facility installed according to the promotion program defined in the Law Concerning Appropriate Operations of Environmental Sanitation Retail Businesses: 8%
- (9) Special depreciation for Advanced Management of Manufacturing Process
Certain machine devices acquired by authorized traders as provided in the Law for Advanced Management of Foodstuff Manufacturing Process: 10% (5% for buildings)
- (10) Special initial depreciation of equipment, etc. used to initiate the re-entry of used goods in the commercial market.
 - (a) Facility for recommercialization of used goods……23%
 - (b) Facility for manufacturing recycling resource utilized products and recycling of specified building material waste……14%
- (11) Increased initial depreciation for machinery or equipment and factory

buildings, used in those areas specified by law.

The specific areas and the special depreciation rates are as follows:

- (a) Peninsular areas for industrial promotion: machinery·····10%, factory buildings·····6%
- (b) Depopulated areas, etc. : machinery·····11%, factory buildings·····7%
- (c) Solitary islands for industrial promotion: machinery·····10%, factory buildings: 6%
- (d) Areas for advanced industrialization in Okinawa: machinery and equipment·····34%, factory buildings·····20%
- (e) Free trade zones and special free trade zone in Okinawa : machinery ·····50%(25% for factory buildings)
- (f) Solitary islands in Okinawa : hotels·····8%
- (12) Special depreciation of the equipment for medical treatment
 - (a) 14% special depreciation of the acquisition cost of medical equipment, etc. (certain emergency medical equipment·····20%)
 - (b) Five-year additional depreciation for specific medical building (Treatment-type clinical building and building for senile dementia disorder treatment ward: 8%)
 - (c) 15% special depreciation of the standard acquisition cost of the building for reconstruction of a hospital etc.
- (13) Special measure that 35% of afforestation cost is deductible as expense
- (14) Special initial depreciation for specific investment, etc. (see 3/8, 1. a)

c. Additional Depreciations

- (1) Special additional depreciation of 27% of ordinary depreciation deductions for the first five years on machinery etc. , used by specific small and medium sized enterprises which execute the programs for strengthening fundamental condition of management stipulated in Special Measures in Promoting Okinawa Prefecture Law.
- (2) (a) Special additional depreciation of 24% of the ordinary depreciation deductions on machinery, etc. (or 32% for factory buildings etc.) of a corporation.
 - (b) Special depreciation of facilities for the handicapped Elevator, etc.: 15% Bus or taxi with lift, etc. : 20% of standard acquisition cost
- (3) An increased depreciation corresponding to 20% of the ordinary depreciation allowed for agricultural machines, equipment, buildings, and animals acquired by agricultural corporations that have expanded their scales in accordance with Plans to Improve Agricultural Management. This depreciation is effective for the first five years from the authorization of the plan.

- (4) Special additional depreciation on good houses for rent etc. .
 - (a) Increased depreciation for good houses for rent in centered urban areas subject to the Law of Revitalization of centered urban areas of 36% for five years (50% in the case of houses with a useful life of 35 years or longer) of ordinary depreciation deductions for the first five years.
 - (b) Increased depreciation for good houses for the aged for rent subject to the Law of Stable Dwelling for the Aged: 36% for five years (good houses for the aged for rent with a useful life of 35 years or longer: 50%)
 - (c) Expenses of remodeling (capital expenditure) to reform existing building stock to residence for rent: 10% Special depreciation
- (5) Special additional depreciation of 10% (50% for the buildings for Project) of ordinary depreciation deductions for the first five years on qualifying buildings etc. used for the purpose of redevelopment of certain areas.
- (6) Special additional depreciation of 12% of ordinary depreciation deductions for the first five years on buildings used as warehouses etc.

3. Reserves

a. Reserve for Overseas Investment Loss

When a corporation acquires the stocks of corporations mentioned below or acquires claims to these corporations under specific conditions, it is allowed for the corporation to deduct the amount of the transfers as an expense, which is made within a certain percentage of the acquisition cost of the stocks or claims to prepare for possible losses arise from a decline in the stock prices. The amount credited to the reserve may be held for five years, but after the sixth year one-fifth of such an amount should be added back to the income in the five succeeding years.

- (a) Natural resource development company.....A company that is exclusively engaged in prospecting, development, or extraction of natural resources abroad (including activities such as those of petroleum companies in Japan) or a foreign government (including a corporation managed by it) that is engaged in such activities,30%
- (b) Natural resource development investment company.....A company that is exclusively engaged in investing (in the form of stockholdings or long-term loans) in a “natural resource development company” or making such investments to develop natural resources.....30%
- (c) Natural resource prospecting company.....A “natural resource development company” that is engaged in the prospecting of natural resources and in land surveying for afforestation, etc.....100%
- (d) Natural resource prospecting investment company.....A “natural

resource development investment company” that is mainly engaged in making investments in a “natural resource prospecting company” or making such investments for the prospecting of natural resources……100%

b. Reserve for Prevention of Mineral Pollution in Metal Mining, etc.

The deduction accumulated by the Metal Mining Agency of Japan in accordance with the Special Measures Law for Prevention of Mineral Pollution in relation to Metal Mining, etc., is deductible as a reserve for the prevention of mineral pollution in relation to metal industries, etc.

c. Reserve for Prevention of Certain Disasters

This reserve is intended to provide for the cost of preventing disasters caused by quarrying, waste disposal, or strip mining after withdrawal, and the expense of maintenance and management of special wastes after their reclamation at the final disposal site.

d. Reserve for Large-scale repair of Shinkansen railways

The reserve accumulated according to the approved reserve plan is included in loss in order to prepare for large-scale repair of Shinkansen railways.

e. Reserve for Loss in Buying Back Computers

Reserve for loss in buying back computers is for computer makers (including sales companies) when they are obliged to buy back specific equipment.

This reserve is counted as loss within a specified limit.

f. Reserve for Reprocessing Used Fuels

The reserve for reprocessing used nuclear fuels is appropriated to reprocessing costs of used nuclear fuels discharged from power generation. The reserve is counted as loss within a specified limit.

g. Reserve for the Removal and Disposal of Atomic Power Generation

Electric facility business enterprises can accumulate reserve within a certain limit and count the sum as loss. When removal is completed and the cost is paid up, the remaining reserve can be counted as income.

h. Reserve for Extraordinary Casualties

The reserve for extraordinary casualties is accumulated by insurance companies for catastrophic loss. This reserve is counted as loss within a specified limit.

i. Reserve for Kansai International Airport Adjustment or Reserve for Central Japan International Airport Adjustment

The reserve for Kansai International Airport adjustment or the reserve for Central Japan International Airport adjustment are accumulated by Kansai International Airport Co., Ltd. and Central Japan International Airport Co., Ltd. as expenses for airport adjustment. The reserves are counted as loss within a specified limit.

j. Special Reserve for Repairs

The sum respectively accumulated for preparing for special repairs of ships, furnaces, and other specified fixed assets is included in loss.

k. Reserve for the contribution to society and community

If Japan Post makes transfer to the reserve for the contribution to society and community which is stipulated in the Japan Post Law, to prepare for an outlay of the reserve within an allowable limit, this transfer is allowed as an expense.

l. Reserve for Locating New Mineral Beds in Japan and Abroad

Mining corporations may reserve the specified amount of money (12% of the sales of minerals as long as it does not exceeds 50% of income which is derived from the sales of minerals) in order to bear the cost of locating new mineral beds in Japan and the abroad. This reserve may be deducted as an expense in computing the taxable income for the accounting period concerned.

The deduction accumulated from this reserve should be withdrawn and added back to the income if (1) the special deduction for the cost of new mineral deposits is applied, or (2) three years have passed after the amount was reserved. When a corporation having a prospecting costs reserve withdraws and disburses new mineral deposit prospecting costs or when a corporation having an overseas prospecting costs reserve withdraws and disburses new overseas mineral deposit prospecting costs, the amount withdrawn may be deducted as an expense in computing the taxable income again. In the other words, the lowest of the following three amounts may be additionally deducted from taxable income in the accounting period in which such costs are disbursed:

- (a) The amount of the prospecting costs incurred, including depreciation expenses allowed for machinery and equipment used for prospecting.
- (b) The amount added back to the income from the prospecting costs reserve.
- (c) The amount of corporation income in the accounting concerned.

Therefore, the deferment provided at the time of deposit may be converted into an income exemption.

m. Reserve for Utilization and Accumulation of Farmland

This reserve is intended to provide for the costs of utilizing and accumulating farmland according to the regulation for utilizing specified farmland in “the law to reinforce fundamentals of agricultural management.” The deductible reserve is 9% of the income from agriculture.

4. Other Special Taxation Measures

a. Special Additional Tax on Capital Gains from Sale or Transfer of Land, etc.

(1) The holding period is 5 years or less:

The gain is taxed at a rate of 10% in addition to ordinary corporation tax.

(2) Other

The gain is taxed at a rate of 5% in addition to ordinary corporation tax.

The measures stated under the above (1) and (2) are suspended from 1998 to 2008.

b. Special Rule for Replacement of Business Assets (Tax Deferral)

If a corporation sells buildings or land, located in a certain specified area, such as a already urbanized area, and buys similar property located in another specified area, within the accounting period in which such a sale is made and places the new property in service within one year of the date of acquisition, 80% of the capital gains may be deferred by reducing the book value of the new assets. If a replacement asset was not purchased by the end of the accounting period in which the sale was made but purchase is intended within one year of the beginning of the next accounting period and the asset is to be placed in service within one year of the date of acquisition, 80% of the expected acquisition cost of the replacement asset multiplied by the profit ratio (the ratio of the gain from the sale to the transferred price) can be deducted as a special account. If a replacement asset was purchased, the amount that is appropriated to the purchase in the special account should be added back to the income. 80% of the acquisition cost of the replacement asset multiplied by the profit ratio can be reduced from the book value of the replacement asset and can be deducted from taxable income.

If the properties mentioned above are exchanged, the same provisions as mentioned are applied.

These special measures are not applied to the land applied of additional

capital gain system on land, etc, held for short time not more than 5 years.

These special measures are designed as part of the national land policy (coping with urban population problems and facilitating industrial zone planning and the efficient use of land) and for other purposes.

The above treatment is granted to the transfer of ships that meet certain qualifications.

c. Special Taxation of Capital Gains from Expropriated Properties

Gains from expropriated properties are the gains derived from the involuntary alienation of properties through the force of laws and regulations. Since it is inappropriate to impose tax on gains from involuntary transfer because of the character of the transaction, preferred tax treatment is prescribed under specified conditions.

If an asset is expropriated and a new asset is acquired in lieu of the expropriated asset within two years from the date of such expropriation, a corporation can elect a special deduction up to 50 million yen or a tax deferral by keeping the acquisition cost of the exploited asset as that of the new asset.

If the acquisition cost of the new asset is more than the book value of the expropriated asset, the special deduction is the lesser of the (1) the value of new asset minus the book value of the expropriated asset or (2) 50 million yen.

If a replacement asset is not acquired by the end of the accounting period in which the expropriation was made, the expropriation proceeds must be shown in a special account.

d. Other Special Deductions for Capital Gains from Land

A deduction of ¥20 million applies to the sale of land to the Urban Development Corporation, or to local or national government, under the laws relating to land.

Corporations that sell land to persons who carry on the business of developing land for housing are granted a deduction of ¥15 million.

A special deduction of ¥8 million applies to the transfer of agricultural land, etc., by a corporation engaged in agricultural production for the purpose of the rationalization of agricultural land holding.

These special deductions are also applied to individual income tax.

e. CFC Tax Measure *

CFC tax measure legislation was introduced in 1978. Under this tax measure, the undistributed income of a foreign subsidiary with a tax burden

* The legislation also includes measures applicable to individuals.

that is significantly lower than the tax burden on corporate income in Japan is added to the income of a domestic corporation in proportion to that corporation's direct and/or indirect ownership of the foreign subsidiary's stock when a foreign subsidiary issued stocks with different claims for dividends, in proportion to the amount of money received on that claims. The undistributed income of a foreign subsidiary is added to the income of a domestic corporation when it owns directly and/or indirectly 5% or more of the issued stock (excluding shares which do not contain rights to dividends and treasury stocks owned by overseas subsidiaries) of the foreign subsidiary and when more than 50% of the total issued stock, issued stock with the right to vote, or issued stock with the right to dividends of the subsidiary is owned directly and/or indirectly by domestic corporations and residents and the tax burden on taxable income of the foreign subsidiary is 25% or less. Stock ownership conditions are judged at the end of the business year for the foreign subsidiary. However the undistributed income of a foreign subsidiary is not added to the income of a domestic corporation, in the year when the foreign subsidiary satisfies all of the conditions below. The amount, which is derived by deducting 10% of certain personnel expenses from the undistributed income, is added if (1) to (3) of the following criteria are satisfied while (4) is not.:

- (1) The main business of the foreign subsidiary is not holding stocks, offering patents, etc., or copyrights, etc., or leasing vessels or aircraft.
- (2) The foreign subsidiary has a fixed facility such as an office, shop, or factory that is deemed necessary to conduct its business in the country or area where its head or main office exists.
- (3) The foreign subsidiary conducts management and control of its business by itself in the country or area where its head or main office exists.
- (4) In a case where the main business of the foreign subsidiary is wholesaling, banking, trust management, securities, insurance, shipping, or air transport, the foreign subsidiary conducts its business mainly with persons other than related persons.*

In a case where the main business of the foreign subsidiary is other than those stated above, the foreign subsidiary conducts its business mainly in the country or area where its main office exists.

When a domestic corporation receives dividends etc., from undistributed

* Persons related to the foreign subsidiary are defined as follows:

- 1) Domestic corporations, consolidated corporations and residents as per legislation.
- 2) Domestic corporations, consolidated corporations and residents that own 50% or more of the total stock of the domestic corporations of 1).
- 3) Affiliated persons of 1) and 2).
- 4) In the case of indirect ownership of stocks of the foreign subsidiary through other foreign corporations, these other foreign corporations and their affiliated persons.
- 5) Affiliated persons of the foreign subsidiary.

income of foreign subsidiary which is calculated as profit, the amount of money correspond to the dividends is allowed as financial loss in calculating profits of domestic corporation.

f. Transfer-Pricing Taxation

- a.** As the globalization of business transactions has proceeded, the possibility of the shift of income abroad through transactions with foreign-affiliated persons has also grown (Transfer-Pricing Problem).

In order to deal with this transfer-pricing problem and to realize fair and legitimate taxation in the field of international transaction, transfer-pricing taxation provisions were introduced in 1986.

- b.** The basic structure of these provisions is as follows:

- (1) In the event that a corporation has conducted the sale or purchase of assets, provision of services, or other transactions with foreign affiliated persons, if the proceed of such transactions is not at an arm's length price, and if this results in a reduction of the income of the corporation, the transactions shall be deemed to have been carried out at an arm's length price for the purpose of corporate income taxation.

In the above,

- (a) foreign-affiliated persons refer to foreign corporations that have one of the following special relationships with said corporation:
- (i) A relationship in which either of two corporations owns, directly or indirectly, a number of shares or an amount of contributed capital comprising 50% or more of the total number of issued shares or total amount of contributed capital of the other corporation (Holding-company relationship).
 - (ii) A relationship in which a number of shares or an amount of contributed capital comprising 50% or more of the total number of issued shares or total amount of contributed capital of two corporations are owned, directly or indirectly, by the same person.
 - (iii) A relationship in which either of two corporations can, in substance, determine all or a portion of the business policies of the other corporation (Substantial-control relationship).
 - (iv) A relationship in which either of two corporations dominates indirectly the other corporation with Holding company or substantial control relationship.
 - (v) A relationship in which both corporations are dominated by the same entity with Holding company relationship or substantial control relationship.
- (b) The arm's length price shall mean the amount that is computed in

accordance with a method listed in the following paragraphs, depending upon the type of transaction in question listed in the following paragraphs:

- (i) Sale or purchase of inventory assets: the following methods (The method listed in D can be employed only in cases where the methods listed in A through C cannot be used):
 - A. Comparable Uncontrolled Price Method: the method which uses, as the amount of consideration in the transaction, an amount equivalent to the amount of consideration in a transaction in which a seller and a buyer, who were not in a special relationship, engaged in sales of inventory assets of the same type as the inventory assets involved in the transaction, under circumstances where the commercial level, transaction volume, etc, are similar (including the consideration amount after making adjustments, in the event that there is a transaction in which said inventory assets of the same type were sold under circumstances where the commercial level, transaction volume, etc, are different and it is possible to adjust the variance in the consideration amount rising due to such differences;
 - B. Resale Price Method: the method that uses, as the consideration amount in the transaction, an amount computed by deducting a normal amount of profit (meaning an amount computed by multiplying the resale price by a normal profit percentage), from the consideration amount with which a buyer of inventory assets involved in the transaction resells said inventory assets to a person with which it has no special relationship;
 - C. Cost Plus Method: the method that uses, as the consideration amount in the transaction, the amount computed by adding a normal amount of profit (meaning an amount computed by multiplying the costs by a normal profit percentage) to the amount of the costs for the seller to acquire by purchase, manufacture, or other acts the inventory assets involved in the transaction and;
 - D. A method similar to the methods listed in A through C above, and other methods prescribed by cabinet order*.
- (ii) Transactions other than inventory: The methods listed below (the methods listed in B can be employed only in cases where the methods listed in A cannot be used.) :

* The transactional net margin method and the profit split method are defined in Government Ordinances.

Corporation Tax (Corporate Income Tax)

- A. A method that is equivalent to methods listed in A through C in the preceding paragraph
 - B. A method that is equivalent to a method listed in D of the preceding paragraph
- (2) The difference between the actual consideration amount in the transaction and the arm's length price prescribed in (1) pertaining to the transaction shall not be deductible in computing the amount of taxable income for the business year for the corporation.
- (3) When tax authorities have requested the corporation to show or provide records, books or copies thereof, as are recognized to be necessary for computing the arm's length price in connection with the transactions for the business year, in case the corporation does not provide those materials without delay, the District Director shall be able to correct or determine the amount of income for said business year for the corporation by presuming the arm's length price to be that amount that is computed in accordance with methods listed above in (1) (b) (i) B and C or other methods prescribed in the cabinet orders as set forth in (i) D (these methods can be used only when the methods described in (i) B, C cannot be applied), using as the basis the gross margin ratio of the business activity of a corporation engaging in a business activity that is of the same type as the business activity involving the transaction of the corporation and where the scale and other details of the business activity are similar.
- (4) When a corporation does not show or provide records or books without delay and it is necessary in connection with an audit concerning transactions between the corporation and a foreign-affiliated person of the corporation, tax authorities shall be able to request from the corporation to disclose or submit records, books or copies thereof, over which the foreign-affiliated person maintains custody. In this case, the corporation shall endeavor to obtain the records and books or copies thereof.
- (5) When a corporation does not show or provide records, books, or copies thereof without delay and if it is necessary in order to compute the arm's length price in connection with the transactions between said corporation and a foreign affiliated person of said corporation, tax authorities shall be able to interrogate or inspect a corporation in the same kind of business with the corporation.
- (6) A corporation shall, in the event it has conducted transactions with a foreign-affiliated person in the corporation during the business year, attach to its final tax return for the business year a document that contains the name and location of the head or main office of the foreign

affiliated person and other items prescribed by ministerial order of the Ministry of Finance.

- (7) Correction and determination with respect to transfer-pricing taxation can be made by tax authorities for six years (generally five years) after the deadline for filing the final tax return.

c. Correlative Adjustment

In the case where a transaction takes place between an enterprise in country A and its related enterprise in country B, the application of transfer-pricing taxation to the related enterprise in country B and a resultant upward revision of its income based on the arm's length principle may give rise to double taxation on those two related enterprises, taken as a single economic entity, so long as the related enterprise is liable for tax on an amount of income that has already been taxed in the hands of the enterprise in country A.

A downward adjustment of income of the enterprise in country A to eliminate such double taxation is generally called "correlative adjustment." Based on the tax treaty with respect to the consideration amount on which the taxable income should be assessed, Japan has a policy of making such correlative adjustments to its enterprises when a mutual agreement with the taxing authority of the country where the related enterprise is located is reached.

However, how the adjustment is made is not fully provided for in tax treaties. Therefore, along with the introduction of transfer-pricing taxation provisions, a provision concerning correlative adjustment is prescribed in article 7 in the Law Concerning Special Rules for Income Tax Law Regarding the Implementation of Tax Treaties.

According to this article, correlative adjustment in Japan is made when the following conditions are satisfied:

- (1) The taxable income of a resident of one of the contracting states other than Japan (country A, hereafter) has been determined pursuant to the provisions of the laws of country A, taking as the basis the consideration amount differing from the actual amount in a transaction between a resident of Japan and said resident of Country A.
- (2) The Finance Minister comes to an agreement based on the provisions of the tax treaty with the competent authority of Country A with respect to the consideration amount with which taxable income will be determined.
- (3) The resident in Japan requests correction of his or her taxable income, while accepting the above-mentioned agreement between the competent authorities.

g. Thin Capitalization Rules

When a foreign or foreign-owned domestic corporation (or when a foreign-owned Japanese corporation) raises funds from foreign-related persons (its parent corporation), the domestic tax burden of the corporate group can be reduced artificially by substituting debt finance for equity finance because the payment of interest can be deducted from the taxable corporate income, while the payment of dividends cannot. This form of international tax avoidance is known as thin capitalization. The purpose of thin capitalization rules is to prevent foreign or foreign-owned domestic corporations from reducing their tax burden through thin capitalization.

The fundamental points of the thin capitalization rules are as follows:

If a corporation's debt to its foreign dominant shareholders and fund providers etc. exceeds 300%, (200% in case of deducting debt related to certain bond repurchase agreements), or an arm's length ratio of the share capital paid in by such foreign dominant shareholders, an interest payment and other payments corresponding to the excessive portion of the debt cannot be deducted for the purposes of corporation tax in the taxable year concerned. However, it is required that the ratio of the corporation's total debt to its total equity exceeds 300% (200% in case of deducting debt related to certain bond repurchase agreements).

The amount of interest payment and other payments which cannot be deducted is calculated as follows:

- ① When the standard average balance of debt is equal to or not more than 300% of the share capital paid in by foreign dominant shareholders;

$$\begin{array}{l} \text{Guarantee charge etc.} \\ \text{corresponding to debt to} \\ \text{domestic fund providers} \end{array} \times \frac{\text{Excessive portion of average balance of} \\ \text{Average balance of debt corresponding} \\ \text{to debt to domestic fund providers}}$$

- ② When the standard average balance of debt exceeds 300% of the share capital paid in by foreign dominant shareholders;

$$\begin{array}{l} \text{Guarantee charge etc.} \\ \text{corresponding to debt to} \\ \text{domestic fund providers} \end{array} + \left[\begin{array}{l} \text{Interest payment and other expenses} \\ \text{corresponding to debt to foreign} \\ \text{dominant shareholders, and fund} \\ \text{providers} \end{array} \right] -$$

$$\left. \begin{array}{l} \text{Guarantee charge, etc.} \\ \text{corresponding to debt to} \\ \text{domestic fund providers} \end{array} \right\} \times \frac{\text{Excessive portion of} \quad \text{Average balance of debt} \\ \text{average balance of} \quad \text{— corresponding to debt to} \\ \text{debt} \quad \text{domestic fund providers}}{\text{Standard average balance of debt}}$$

The standard average balance of debt is defined as the average balance of the debt owed to other than domestic fund providers, out of the debt owed

to foreign dominant shareholders and fund providers. Foreign dominant shareholders are defined as nonresident individuals or corporations, ①who own directly or indirectly 50% or more of the total equity of the corporation, or ② who control the corporation in other ways (including effective control), or ③ who are controlled by the same persons who control the corporation.

The amount of the share capital paid in by the foreign dominant shareholders is derived by multiplying the difference between the average balance of the corporation's total asset and that of its total debt, by the ratio of shares hold by the foreign dominant shareholder directly or indirectly to the total shares of the corporation. The difference mentioned above should be at least as large as the amount of capital etc. (capital and capital reserve defined in the corporation tax law), which will be called the amount of equity hereafter. The average balance of net total asset and debt should be calculated rationally.

Fund providers are defined as persons who provide funds to domestic corporations, or persons who are involved in the provision of the funds. The guarantee charge etc., is defined as the debt guarantee charge and the usage fees of bonds paid to foreign dominant shareholders.

Excessive portion of average balance of debt is derived by deducting the amount three times as much as the amount of equity provided by foreign dominant shareholders, from the average balance of debt corresponding to debt to foreign dominant shareholders and fund providers. Interest payment is defined as interest payments on debt and guarantee charges.

The amount of the share capital provided by the foreign dominant shareholders in the above formula is the difference between the book value of the average balance of the corporation's total asset and that of its total debt times the percentage of the foreign affiliated persons' direct and indirect holding of the total shares of the corporation. The difference mentioned above should be at least as large as the amount of capital, etc. (capital is capital reserve defined by the corporation tax law), which will be called the amount of own capital hereafter. The average balance of total asset or debt should be calculated rationally.

If the corporation proves that its debt/equity ratio is reasonable in comparison with those ratios of other corporations in similar size conducting similar business, such an arm's length ratio will be used in applying the thin capitalization rules instead of 300% or 200%

In the case of foreign corporations, the necessary adjustment is made, i. e., the owned capital is the difference between the total assets relating to domestic activities and the total debt relating to domestic activities. The same adjustment is made for the share capital paid-in by foreign-affiliated

persons.

This provision of the capitalization is applied to the accounting years since April, 1. 1992.

3/9 Income Examination

1. General Investigation Procedures

Corporation tax returns are investigated in much the same way as in the case of individual income tax returns. Tax officers examine corporations' account books and question corporate officers whenever necessary. They may also pose questions to those paying money or transferring assets to the corporation or those receiving money or assets from the corporation. In some cases, they may inspect the books and records of such third parties with respect to transactions with the corporation under investigation.

2. Corporations under the Jurisdiction of the Examination Department

Jurisdiction for investigations of corporate returns is distributed between the Auditing Departments of Regional Taxation Bureaus and the Tax Offices. In principle, the Auditing Department of a Regional Bureau is in charge of corporations with capital of ¥100 million or more and foreign corporations; the Tax Office is in charge of domestic corporations with capital of less than ¥100 million.

CHAPTER IV

INHERITANCE TAX AND GIFT TAX

4/1 General

The inheritance tax was established in 1905 and was originally an estate tax, the tax base of which was the value of a decedent's properties. The tax retained its original nature until 1949, but was changed in 1950 to an accession tax in accordance with the recommendations of the Tax Mission led by Dr. Carl Shoup. This accession tax was imposed on the recipient of inherited properties, gifts, or bequests, and the value of properties used as the tax base was computed cumulatively over the recipient's lifetime. In the 1953 amendments, the accession tax was divided into the inheritance tax and gift tax, and the method of cumulative taxation was repealed.

The gift tax was imposed to complement the inheritance tax. Without the gift tax, a decedent could distribute his/her properties to successors prior to his/her death in order to avoid or lessen the inheritance tax burden.

In 1958, the system of inheritance and gift taxes was revised. Under the former system, each heir or donee was liable for the tax on property received, and the distribution of properties among heirs could make a great difference in the inheritance tax burden. In some cases, distribution was made only out of tax considerations.

Under the present system, the amount of inheritance tax is based on the number of statutory heirs and statutory share of each heir. The table below shows the status of inheritance and gift tax in 2004.

Revenue from the Inheritance Tax and Gift Tax

Inheritance Tax		Gift Tax	
Heirs with taxable property	(persons) 131,279		
Their descendants	43,488		
Number of heirs taxed	111,820	Number of donees taxed	(persons) 403,814
Taxable amount of property	(billion yen) 9,862	Taxable amount of property	(billion yen) 2,310
Amount of inheritance tax	1,065	Amount of gift tax	97

4/2 Taxpayers

1. An individual who acquires property by inheritance, bequest, or gift and who has domicile in Japan at the time of acquisition
2. An individual who acquires any property located in Japan by inheritance, bequest, or gift and who has no domicile in Japan at the time of acquisition
3. A person who acquires properties by inheritance and meet all the requirements stated below
 - a. having a domicile outside of Japan
 - b. having Japanese nationality
 - c. having acquired properties or otherwise from the person who had a domicile in Japan within five years before the inheritance or gift
4. An individual who acquires property by gift, on which the taxation system for settlement at time of inheritance is applied

4/3 Inheritance Tax

1. Tax Base

The inheritance tax is imposed on the total value of all properties (including acquired properties by gift, on which the taxation system for settlement at time of inheritance (4/5) is applied) acquired through inheritance or bequest, less liabilities and funeral expenses. Properties are appraised based on current prices or values at the time of acquisition.

The following items, however, are not included in the tax base:

- a. The amount of such properties acquired through inheritance or bequest by a person engaged in religious, charitable, scientific, or other activities for the public welfare when these properties will be used for public purposes.
- b. The right to receive payments from mutual aid systems for the handicapped carried out by local public entities according to their regulations.
- c. Life insurance and personal accident insurance proceeds received by heirs by reason of the decedent's death (maximum: ¥5,000,000 × number of statutory heirs).
- d. Retirement and similar allowances (the payment of which is decided within three years after the death of the decedent) received by heirs by reason of the decedent's death (maximum: ¥5,000,000 × number of statutory heirs).

2. Basic Exemption

¥50 million + (¥10 million × number of statutory heirs)

In computing the amount of basic exemption and the limit of non-taxable life

insurance, etc. the number of adopted children included as statutory heirs is limited to one if there is a biological child, or to two if there is not.

3. Calculation of Tax Amounts

a. Calculation of Total Tax

If any heirs or legatees received gift properties from the descendant within three years prior to the inheritance, the value of such gift properties is included in the tax base for inheritance tax.

First, the amount of the basic exemption described in **2.** above is subtracted from the value of total properties inherited or bequeathed to obtain the amount of taxable properties.

Second, the amount of taxable properties is attributed to each heir corresponding to the number of statutory heirs in accordance with the statutory share prescribed in the Civil Code* irrespective of the actual share. In calculating the total inheritance tax liability, the number of adopted children included as statutory heirs is limited to one if there is a biological child or to two if there is not.

Third, the value of properties attributed to each heir, corresponding to the number of statutory heirs, is multiplied by the corresponding tax rate; the tax so computed for each statutory heir is then added to obtain the total tax amount due.

b. Distribution of Total Tax

The total tax computed in **a.** above is distributed to each heir and legatee in proportion to his or her actual share to obtain the tax amount due.

c. Additional Tax for Certain Legatees and Heirs

If the heir or legatee is a person other than a spouse, child (including heirs by representation), or parent of the decedent, 20% of the inheritance tax distributed in **b.** above, is added thereto.

d. Tax Credits for Certain Heirs

(1) If an heir or legatee received gift properties from the decedent three years before his or her death and the value of such properties is included in the value of total properties inherited or bequeathed, the gift tax with respect to such properties is credited with respect to the inheritance tax due for the heir or legatee.

(2) If a surviving spouse received properties, he or she may deduct from his

* The distribution of an estate to statutory heirs as provided for in the Civil Code is as follows:

lineal descendants	1/2 of an estate	spouse	1/2
lineal ascendant	1/3	spouse	2/3
brothers and sisters	1/4	spouse	3/4

This portion is equally attributed among heirs of the same category in all instances.

Inheritance Tax and Gift Tax

or her inheritance tax liability the amount indicated below:

$$\left[\begin{array}{l} \text{Total} \\ \text{inheritance tax liability} \end{array} \right] \times \frac{\left[\begin{array}{l} \text{The lesser of: ① the statutory share of the} \\ \text{surviving spouse of the value of net total} \\ \text{properties bequeathed (minimum ¥160} \\ \text{million) or ② net amount of properties} \\ \text{actually received by the surviving spouse} \end{array} \right]}{\left[\text{The value of the total properties bequeathed} \right]}$$

- (3) If the heir is a minor under the age of 20, the product of ¥60,000 multiplied by the difference of his or her age and 20 is deductible from such heir's inheritance tax.
- (4) If the heir is handicapped, the product of ¥60,000 (¥120,000 in the case of the severely handicapped) multiplied by the difference of his or her age and 70 is deductible from such heir's inheritance tax.
- (5) If the decedent received the properties by inheritance within ten years before his or her death, a certain percentage of inheritance tax imposed on the decedent is deductible from the inheritance tax imposed on the heir who receives the properties of that decedent.
- (6) In case a successor paid gift tax under the taxation system for settlement at the time of inheritance, the successor can deduct the amount of the paid gift tax from the inheritance tax imposed at the time of the inheritance from the donor.

4. Tax Rates

Inheritance Tax Rates

Taxable Amount for each Heir	Tax Liability	
not over		
¥ 10,000,000	10% of taxable amount	
¥ 30,000,000	15% of taxable amount minus	¥ 500,000
¥ 50,000,000	20% of taxable amount minus	¥ 2,000,000
¥ 100,000,000	30% of taxable amount minus	¥ 7,000,000
¥ 300,000,000	40% of taxable amount minus	¥ 17,000,000
over		
¥ 300,000,000	50% of taxable amount minus	¥ 47,000,000

Example of inheritance tax calculation

Descendant: Mr. X

Heirs: Mrs. X

Messrs. Y₁ and Y₂ (descendant's children)

Total value of properties bequeathed ¥800,000,000 (A)

Value of properties inherited by each heir	Mrs. X ¥400,000,000 (B)
	Mr. Y ₁ ¥200,000,000 (C)
	Mr. Y ₂ ¥200,000,000 (D)

Calculation of tax amounts

- (1) Amount of basic exemption for inherited properties

$$¥50,000,000 + ¥10,000,000 \times 3 = ¥80,000,000 \text{ (E)}$$

- (2) Tax base (A - E)

$$¥800,000,000 - ¥80,000,000 = ¥720,000,000 \text{ (F)}$$

- (3) Total amount of tax

Tax base	Statutory share of inheritance	Corresponding tax amount
¥720,000,000 (H) × (Mrs. X)1/2	= ¥360,000,000	¥133,000,000 (G)
¥720,000,000 (H) × (Mr. Y ₁)1/4	= ¥180,000,000	¥ 55,000,000 (H)
¥720,000,000 (H) × (Mr. Y ₂)1/4	= ¥180,000,000	¥ 55,000,000 (I)
Total amount of tax (G + H + I) = ¥243,000,000 (J)		

- (4) Tax amount to be paid by each heir

$$\begin{aligned} \text{Mrs. X} \quad & ¥243,000,000 \text{ (J)} \times \frac{¥400,000,000}{¥800,000,000} - ¥243,000,000 \\ & \times \frac{¥400,000,000^*}{¥800,000,000} = 0 \\ \text{Mr. Y}_1 \quad & ¥243,000,000 \text{ (J)} \times \frac{¥200,000,000}{¥800,000,000} = ¥60,750,000 \\ \text{Mr. Y}_2 \quad & ¥243,000,000 \text{ (J)} \times \frac{¥200,000,000}{¥800,000,000} = ¥60,750,000 \end{aligned}$$

5. Special Rules for Calculation of the Tax Base with Respect to Small Sites, etc.

With respect to certain sites for business (less than 400 m²) or certain sites for residence (less than 240 m²), the taxable base is obtained by decreasing 80% or 50% of the respective value.

Note: 1. The total area obtained by redrawing each small-sized residential site as a business site of a certain size shall not be in excess of 400 m².

2. This system may be used together with the special tax treatment for special business assets within the limit of the rate for the part less than the upper limit.

* See 4/3, 3. d.(2)

6. Special Tax Treatment for Calculation of Taxable Value for Special Business Assets

- a.** For stocks without any market price acquired by individuals through inheritance, 10% of the taxable value for inheritance tax is reduced (¥100 million maximum).
- b.** For mountains and forests (growing trees and forest sites) acquired by individuals through inheritance, 5% of the taxable value for inheritance tax is reduced.

Note: 1. This system may be used together with the special tax treatment for small sites within the limit of the rate for the part less than the upper limit

- 2. Also for a gift property, based on the taxation system for settlement at the time of inheritance, the taxable amount can be reduced in settlement at the time of inheritance under this taxation system subject to satisfying certain requirements.

7. Special Tax Treatment for Farmland

Payment of the inheritance tax on farmland acquired by heir or legatee who receives agricultural land from a farmer through inheritance or bequest may be postponed with respect to the difference between the market value of the agricultural land and the value of the land as agricultural land, if the heir or legatee declares on intention to continue agriculture on the land, and the amount of tax whose payment is postponed may be exempted if the heir or the legatee continues agriculture there for 20 years.

If the heir or legatee ceases to use the land for agriculture for which tax payment is postponed within 20 years of inheritance, then the postponement of tax payment described above is withdrawn, and he or she must pay the inheritance tax together with the interest on it.

However, this postponement is not applicable to farmland within the “Urbanization Promotion Areas” in certain cities.

4/4 Gift Tax (Calendar-Year Taxation)

1. Tax Base

Gift tax is imposed on legacies acquired in a calendar year. Properties are appraised on the basis of current prices or values at the time of acquisition. The following items, however, are not included in the tax base:

- a.** Properties acquired from corporations.

(This amount is included in the tax base for income tax as occasional income.
See 2/3, 2. (9).)

- b.** Properties acquired by a person for living and educational expenses from relatives who are responsible for supporting him or her.
- c.** Properties acquired by a person engaged in religious, charitable, scientific, or other activities for the public welfare that meet certain conditions when the properties will be used for public purposes.
- d.** Bounties for science and research granted from certain specific non-profit trusts.
- e.** The right to receive payment from mutual aid systems for the handicapped carried out by local public entities according to their regulations.
- f.** Political contributions reported under the Public Offices Election Act.
- g.** The extent up to ¥60 million of a trust where the beneficiary is severely handicapped.

2. Basic Exemption

¥1,100,000

3. Exemption for Spouses

When a person married for 20 years or longer receives residential properties for his or her own residence, or the money for acquiring such properties from his or her spouse, he or she may be allowed, in addition to the basic exemption, a spousal exemption not exceeding ¥20 million. A spousal exemption, however, may be claimed only once per spouse.

4. Tax Rates

Gift Tax Rates(Calendar-Year Taxation)

Taxable Amount	Tax Liability
not over	
¥ 2,000,000	10% of taxable amount
¥ 3,000,000	15% of taxable amount minus ¥ 100,000
¥ 4,000,000	20% of taxable amount minus ¥ 250,000
¥ 6,000,000	30% of taxable amount minus ¥ 650,000
¥ 10,000,000	40% of taxable amount minus ¥ 1,250,000
over	
¥ 10,000,000	50% of taxable amount minus ¥ 2,250,000

4/5 Taxation System for Settlement at the Time of Inheritance

1. Outline

A person having acquired a property through donation and satisfying certain requirements is allowed to select a taxation system for settlement at the time of inheritance instead of a taxation system for each calendar year (see 4/4). In the said system, the person shall pay gift tax for the donated property at the time of donation, and then pay inheritance tax at the time of inheritance arising afterwards. The amount of the inheritance tax shall be obtained by subtracting the amount of the gift tax already paid from the total amount of the tax payable which is calculated on the basis of the total of the donated property and the inherited property.

2. Taxpayers covered by this taxation system (His/her age is the age as of January 1 of the year when donation takes place.)

(1) Donee

Presumed heirs, twenty years old or older, who are the children of the donor including the children of the heirs in the event they are dead

(2) Donor

A parent who is sixty-five years old or older (specified donor)

3. Special deduction (range of tax-exemption)

¥25 million (applicable for two years or more unless the total deduction reaches the upper limit)

4. Tax amount calculation

(1) At the time of donation

- * Gift tax shall be imposed on the property donated from the specified donor separately from other donated properties
- * Tax shall be imposed, subject to declaration, at the tax rate of 20% on the part of the property in excess of the special deduction (¥25 million).

(2) At the time of inheritance

- * The amount of inheritance tax shall be calculated based on the total of donated properties under this system and the inherited property
- * The amount equivalent to the gift tax already paid shall be deducted from the amount of inheritance tax (see 4/3 “Inheritance Tax” for the method of calculation). (The part of the paid gift tax remaining after the deduction shall be returned.)

(Note): The amount of the donated property to be added to the amount of inherited property shall be in the current price as of the time of donation.

5. Application procedures

- * A notice to the effect that this taxation system was selected shall be attached to the declaration of the gift tax submitted during the period from February 1 to March 15 of the year next to the year of donation.
- * In cases notified at the time of the initial donation, application of this taxation system shall be continued till the time of inheritance.
- * Each of the brothers and sisters as donees can separately select this system for each of their parents (father and mother) as the specified donors.

6. Special cases (applicable till 2007) for acquisition of residence under the taxation system for settlement at the time of inheritance

- * In a case where the capital to acquire a residence or the capital to be appropriated to enlarge or remodel a residence is obtained through donation, the taxation system for settlement at the time of inheritance may be applicable even to the property donated from a parent who is younger than 65 years old.
- * In case the capital to acquire a residence or the capital to be appropriated to enlarge or remodel a residence is obtained through donation, the amount of the special deduction may be extended to ¥35 million (¥10 million to be added).

4/6 Returns and Tax Payment

1. Returns

a. Inheritance Tax

A person who acquires properties by inheritance or bequest must file a return within ten months of the date of inheritance.

b. Gift Tax

A person who acquires properties by gift must file a return between 1 February and 15 March of the following year.

2. Tax Payment

- a.** The inheritance tax and the gift tax must be paid during the filing period or by the last filing day.
- b.** Deferment of payment for up to five years for the inheritance tax or the gift tax is approved in cases where the tax amount exceeds ¥100,000 and there are

Inheritance Tax and Gift Tax

reasons for not paying the amount at one time. If real properties and the right to use land, standing timber, depreciable assets, and non-listed stocks of a family company, of which the heir and the special concerned person have no less than 50% of stocks and constitute no less than 50% of the total amount of inherited properties, the maximum term for payment of the inheritance tax corresponding to real properties, etc. may be extended to 15 years and that corresponding to other properties may be extended to 10 years. If real properties, etc. constitute no less than 75% of the total amount of the properties, the maximum term for payment of the tax amount is extended to 20 years.

If a taxpayer is permitted to postpone the payment of tax, he or she has to pay tax interest at the rate of 6.0, 5.4, 4.8, 4.2, 3.6, or 1.2% per annum, as the case may be. As an exceptional measure, these interest tax rates can be reduced when the official discount rate plus 4% is lower than 7.3%.

- c.** Payment of inheritance tax in kind is approved when it is difficult for the taxpayer of inheritance to pay in cash. In such a case, payment may be made with the inherited or bequeathed properties. By the time payment in kind is completed, interest tax must be paid at the annual rate of 7.3%.

CHAPTER V

LAND VALUE TAX

5/1 General

The land value tax was introduced in 1991 and imposed on land holdings in order to require fair burdens on land holding and to reduce the preference for land among asset holding measures. After 1998, the imposition of the land value tax was suspended.

5/2 Taxpayers

Individuals and corporations who are owners of land, etc., in Japan are required to pay this tax.

5/3 Tax Base

The tax base is the total amount of the assessment value (the assessed value for the Inheritance Tax) of all the land (excluding exempted land listed below) held by a taxpayer as of the first day of each year (taxable period), minus the amount of the basic deduction.

5/4 Basic Deductions and Exemptions ,etc.

1. Basic Deductions

Taxpayers are entitled to deduct the amount indicated in (a) or (b), whichever is larger.

- | | | |
|--|----|--|
| (a) { | 1) | Corporations capitalized at more than ¥1 billion·····¥1 billion
(¥500 million in 1997) |
| | 2) | Corporations capitalized at more than ¥100 million
but not exceeding ¥1 billion·····¥1 billion (¥800 million in 1997) |
| | 3) | Other corporations & natural persons·····¥1.5 billion |
| (b) ¥30,000 multiplied by the area in squared meters of land possessed (※) | | |
| (※) exempted land is excluded. | | |

2. Exemptions ,etc.

Exemptions and reductions of the assessment value for certain land are

Land Value Tax

available as described below:

- a.** Land held by national and local governments or public corporations.
- b.** Land held by public service corporations, etc. (educational or religious associations). Tax will be levied on land used for purposes not directly related to proper activities.
- c.** A lot no larger than 1,000 m² used as the holder's primary residence and building sites rented for residential purposes. This does not include company houses for board directors.
- d.** Land with an assessment value no higher than ¥30,000/m².
- e.** Land used directly for purposes closely connected with public welfare, such as hospitals, social welfare facilities, railways, telephone service, water and electricity supply, etc.
- f.** Agricultural or forest land. As for agricultural land within Urbanization Promotion Areas in designated cities in the three Metropolitan areas and that is not designated as agricultural land to be preserved under the Productive Green Tract Area system, the exemption does not apply.
- g.** The taxable value is reduced to one-fifth of the assessment value in the case of land scheduled to be sold within good-standard home lot development projects or housing construction projects.
- h.** The taxable value is reduced to one-half of the assessment value in the case of land for environmental protection facilities required by regulations under the Factory Location Law and land held by enterprise cooperative associations, agricultural cooperative associations, etc.
- i.** The taxable value is reduced to 2/3 for certain lands, etc.; notably those required to be open to the public as designated by the Buildings Standards Act.

5/5 Tax Rate

The tax rate is fixed at 0.3%. However, special treatment for 1996 and 1997 (0.15%) is applicable.

5/6 Returns and Tax Payment

Taxpayers are to file returns by October 31 of the relevant year. Half of the tax account is to be paid by the date mentioned above, and the rest is to be paid by March 31 of the following year.

CHAPTER VI

REGISTRATION AND LICENSE TAX

6/1 Taxpayers

Registration and license tax is levied on registrations in official books or documents in connection with the acquisition, creation, transfer, alteration, lapse, etc., of rights, or in connection with qualifications for the practice of certain professions and for obtaining a business license. The following, however, are exempt from the tax, for example:

1. Registrations by national and local governments, Incorporated Administrative Agency, the Urban Renaissance Agency, and other government-affiliated agencies.
2. Registrations of sites or buildings of embassies, legations, or consulates of foreign countries that reciprocate the same privileges with Japan.

6/2 Taxable Registration and Licenses

1. Registration of real estate and ships
2. Registration of commercial companies
3. Registration of copyrights, patent rights, utility model rights, design rights, or trademarks rights
4. Registration of lawyers, doctors, certified public accountants, or appraisers of real property
5. License to conduct banking business
6. License to conduct liquor businesses

(Note) The above list does not enumerate all taxable items.

6/3 Tax Base

1. Value of real estate and ships to be registered, etc., in the case of 1 in **6/2** above.
2. Sum of capital, etc. in the case of 2 in **6/2**
3. Number of items to be registered in the case of 3 in **6/2** above.
4. Number of applications for registration and license in the case of 4, 5, or 6 in **6/2** above.

6/4 Tax Rates

Tax rates vary according to the type of assets or the type of registration or license. The tax rates on main items are as follows:

1. Registration of Real Estate

	Tax base	Rate (General rule)
(1) Preservation of ownership	Value of property	0.4%
(2) Transfer of ownership		
(a) By merger or inheritance	Value of property	0.4%
(b) By bequest or gift	Value of property	2.0%
(c) By sale	Value of property	2.0%
(3) Acquisition of surface rights by settlement or lease	Value of property	1.0%
(4) Acquisition of right of pledge or hypothecation	Amount of loan	0.4%
(5) Provisional registration of transfer ownership	Value of property	half of definitive registration
(6) Registration of addition, correction, alteration, or erasure	¥1,000 for each property	
(Note) With regard to the rate of registration and license tax (2)(c), the tax rate shall be reduced to half of general rule as a temporary measure for the period from April 1, 2006 to March 31, 2008 (only applicable to the registration of land).		

2. Registration of Ships

(1) Preservation of ownership	Value of ship	0.4%
(2) Acquisition of property		
(a) By merger or inheritance	Value of ship	0.4%
(b) By bequest or gift	Value of ship	2.0%
(c) By other causes	Value of ship	2.8%
(3) Acquisition of hypothecation	Amount of loan	0.4%

3. Registration of Personal Property

Acquisition of hypothecation	Amount of loan	0.3%
------------------------------	----------------	------

4. Registration of Aircraft

- | | | |
|--|------------------|------|
| (1) New registration or registration of transfer | ¥30,000 per tone | |
| (2) Acquisition of hypothecation | Amount of loan | 0.3% |

5. Registration of Copyrights or Rights of Patent

- | | | |
|--|--|--|
| (1) Transfer of copyrights by sale | ¥18,000 or ¥9,000 (for quasi copyrights) | |
| | per case | |
| (2) Transfer of rights of patent by sale | ¥15,000 per case | |

6. Registration of Commercial Companies

- | | Tax base | Rate |
|--|---|------|
| (1) Incorporation of company | | |
| (a) Stock company | Amount of capital
(at least ¥150,000) | 0.7% |
| (b) Japanese-version LLC (“Godo-Kaisyā”) | Amount of capital
(at least ¥60,000) | 0.7% |
| (c) Unlimited partnership, Limited partnership | ¥60,000 per registration | |
| (2) Increase capital regarding stock companies and limited liability company | amount of capital increased
(at least ¥30,000) | 0.7% |

7. Registration of Lawyers, Doctors, Certified Public Accountants, or Appraisers of Real Property

- | | |
|------------------|--------------------------|
| New registration | ¥60,000 per registration |
|------------------|--------------------------|

8. Licensing of Banking Business, etc.

- | | |
|--|----------------------|
| (1) Licensing of business | ¥150,000 per license |
| (2) Approval of foreign branch establishment | ¥150,000 per branch |

9. Licensing of Manufacture and Sale of Liquor

- | | |
|--------------------------------|-----------------------------|
| (1) Licensing of manufacturing | ¥150,000 per license |
| (2) Licensing of sales | |
| (a) Wholesale and Retail | ¥90,000 per selling premise |

Registration And License Tax

(b) Retail only ¥30,000 per selling premise

10. Permission for Construction Activities

New registration permission ¥150,000 per permission

CHAPTER VII

STAMP TAX

7/1 Taxpayers

The Stamp Tax is imposed on persons who prepare taxable documents such as deeds of contracts, certificates, etc., listed in Annex I of the Stamp Tax Law.

7/2 Tax Rates

The Stamp Tax is imposed on each document. Tax rates are as follows:

Stamp Tax Rates

Document	Amount	Rates
1. Deed of contract concerning transfer of real estate, mining rights, intangible property rights, vessels, aircraft, or a profit-making business; deeds of contract concerning creation or transfer of specialties or lease of land; deeds of contracts concerning loans; and deeds of contracts concerning transportation, including chartering of vessels	Less than ¥10,000	0
	¥ 100,000 or less	¥ 200
	¥ 500,000 or less	¥ 400
	¥ 1million or less	¥ 1,000
	¥ 5million or less	¥ 2,000
	¥ 10million or less	¥ 10,000
	¥ 50million or less	¥ 20,000
	¥ 100million or less	¥ 60,000
	¥ 500million or less	¥ 100,000
	¥ 1billion or less	¥ 200,000
	¥ 5billion or less	¥ 400,000
	Over ¥5billion	¥ 600,000
	If no amount is stated	¥ 200
Among the items above, deeds of contracts concerning transfer of real estate in an amount over 10 million yen	¥ 50million or less	¥ 15,000
	¥ 100million or less	¥ 45,000
	¥ 500million or less	¥ 80,000
	¥ 1billion or less	¥ 180,000
	¥ 5billion or less	¥ 360,000
	Over ¥5billion	¥ 540,000

(continued)

Stamp Tax

Document	Amount	Rates	
2. Deeds of contracts concerning contracting for work	Less than ¥10, 000	0	
	¥ 1million or less	¥ 200	
	¥ 2million or less	¥ 400	
	¥ 3million or less	¥ 1, 000	
	¥ 5million or less	¥ 2, 000	
	¥ 10million or less	¥ 10, 000	
	¥ 50million or less	¥ 20, 000	
	¥ 100million or less	¥ 60, 000	
	¥ 500million or less	¥ 100, 000	
	¥ 1billion or less	¥ 200, 000	
	¥ 5billion or less	¥ 400, 000	
	Over ¥5billion	¥ 600, 000	
	If no amount is stated	¥ 200	
	Among the items above, deeds of contracts concerning contracting for building work in an amount over 10million yen	¥ 50million or less	¥ 15, 000
		¥ 100million or less	¥ 45, 000
		¥ 500million or less	¥ 80, 000
		¥ 1billion or less	¥ 180, 000
		¥ 5billion or less	¥ 360, 000
		Over ¥5billion	¥ 540, 000
3. Promissory notes; bills of exchange	Less than¥100, 000	0	
	¥ 1million or less	¥ 200	
	¥ 2million or less	¥ 400	
	¥ 3million or less	¥ 600	
	¥ 5million or less	¥ 1, 000	
	¥ 10million or less	¥ 2, 000	
	¥ 20million or less	¥ 4, 000	
	¥ 30million or less	¥ 6, 000	
	¥ 50million or less	¥ 10, 000	
	¥ 100million or less	¥ 20, 000	
	¥ 200million or less	¥ 40, 000	
	¥ 300million or less	¥ 60, 000	
	¥ 500million or less	¥ 100, 000	
	¥ 1billion or less	¥ 150, 000	
	Over ¥1billion	¥ 200, 000	
	Bills payable on sight, etc.	¥ 200	

(continued)

Document	Amount	Rates
4. Share certificates; subscription certificates; bond ; and beneficiary certificates	¥ 5million or less	¥ 200
	¥ 10million or less	¥ 1, 000
	¥ 50million or less	¥ 2, 000
	¥ 100million or less	¥ 10, 000
	Over 100million	¥ 20, 000
5. Merger contract, division contract or division plan		¥ 40, 000
6. Articles of incorporation (original only)		¥ 40, 000
7. Deeds of basic contracts for continuous transactions (such as agent contracts)		¥ 4, 000
8. Deposit certificates; bills of lading; insurance certificates; letters of credit; deeds of contracts concerning trusteeship; deeds of contracts concerning trust; and deeds of contracts concerning assignment of obligations, etc.		¥ 200
9.(1) Receipt of money or securities in light of goods or services	Less than ¥30, 000	¥ 0
	¥ 1million or less	¥ 200
	¥ 2million or less	¥ 400
	¥ 3million or less	¥ 600
	¥ 5million or less	¥ 1, 000
	¥ 10million or less	¥ 2, 000
	¥ 20million or less	¥ 4, 000
	¥ 30million or less	¥ 6, 000
	¥ 50million or less	¥ 10, 000
	¥ 100million or less	¥ 20, 000
	¥ 200million or less	¥ 40, 000
	¥ 300million or less	¥ 60, 000
	¥ 500million or less	¥ 100, 000
	¥ 1billion or less	¥ 150, 000
	Over ¥1billion	¥ 200, 000
		¥ 200
(2) Receipt of money or securities other than in (1) above		
10. Bank bankbook		¥ 200
11. Other bankbooks		¥ 400
12. Chit book		¥ 4, 000

7/3 Tax Payment

The Stamp Tax is paid by affixing stamps on a deed, etc., and invalidating the stamps by seal or signature. The stamps are sold at post offices, etc. Instead of affixing stamps, the taxpayer may pay the tax in cash and get an imprint placed on the document by a Tax Office or may file a return and pay the tax after preparing the documents and so on, if prior approval is given by the Director of a Tax Office.

If a taxpayer fails to pay the tax as required by law, the person is subject to penalties.

CHAPTER VIII

CONSUMPTION TAX

8/1 General

Consumption tax is an indirect tax fairly and widely imposed on general consumption. In domestic transactions, taxpayers are business enterprises offering asset transfers, loans and services for consumption and these who receive foreign goods from bonded areas. Consumption tax is added on (shifted) to the price of goods and services offered by enterprises and ultimately borne by consumers. Since this tax is assessed on transactions by enterprises at each manufacturing, wholesale, and retail stage, it contains a scheme for avoiding tax accumulation by way of deducting taxes on purchases, thus making it neutral to industry and the economy in general.

The tax period for the calculation of tax payable on domestic transactions is for individual proprietors, the calendar year which overlaps with the tax period for their income tax returns, and for corporations, the accounting period which overlaps with their corporate tax returns. Calculation of the deductible consumption tax on purchases is based on both book entries and invoices or delivery statements currently in use instead of invoices. For small and medium-sized business enterprises, a simplified taxation system is utilized to alleviate the administrative burden on tax payers, thereby enabling calculation of the tax amount from the sales amount. The rate of tax is a flat 4% (together with the 1% local consumption tax, a local tax, the tax rate reaches 5%). Various amendments were rendered in 1991 notably on the scope of exemption and on the simplified taxation system, which was followed by amendments in 1997 for the introduction of the current flat rate of 4% and abolition of the special deduction system for small and medium-sized enterprises. The reduction of the special measure for small & medium-size enterprises introduced in the FY 2003 reform will be applied from FY2004.

8/2 Taxable Items

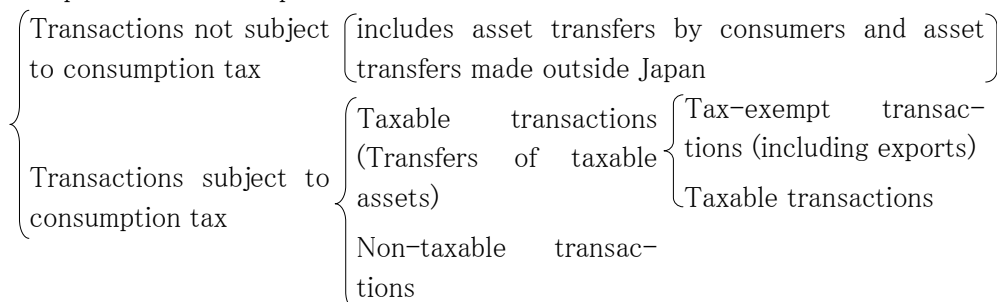
1. General

Consumption Tax Law (hereafter called the “Law”) applies to asset transfers by enterprises in Japan and foreign goods received from bonded areas.

“Asset transfers” mean sales and leasing of assets and provision of services effected for compensation as a business activity. For such asset transfers, taxable items are those effected by enterprises in Japan.

Consumption Tax

Even among asset transfers by enterprises in Japan, there are categories not subject to taxation, the so-called nontaxable transactions. Among taxable transactions, moreover, certain items including export transactions are exempted from consumption tax.



2. Transactions subject to Consumption Tax

Transactions fall within the scope of the law if they are (1) domestic transactions, (2) a business activity, (3) effected for compensation, and (4) categorized as sales and leasing of assets or provision of services.

(1) Domestic transactions

The consumption tax is levied only on transactions made in Japan. Therefore, in cases where enterprises have transferred assets purchased in foreign countries to third parties without bringing them into Japan, such transactions are not subject to taxation.

The criteria for judging whether or not a transaction has been made in Japan are shown elsewhere in this section.

(2) Business activity

Consumption tax is levied only on transactions made as a business activity. This leaves sales of household assets by an individual entrepreneur free from taxation.

In addition, taxable asset transfers shall include the sales and leasing of assets and the provision of services effected for compensation in conjunction with business activities.

(3) Effected for compensation

Consumption tax is, in principle, levied only on transactions made for compensation. The activities shown below are regarded as asset transfers effected for compensation as a business activity.

(a) Consumption or use, for household purposes by an individual entrepreneur, of inventory or other assets that have been used for business purposes and;

(b) Gift assets by a corporation to its directors.

As explained above, taxable items only include transactions made for

compensation. Therefore, excluded from taxation are activities such as the use and consumption of merchandise or raw materials for purposes including advertisement, other publicity, and research and development conducted directly by the enterprise.

Insurance proceeds received, dividends received (limited to those related to capital contributions), and compensation for damages inflicted on persons or assets do not fall under compensation related to asset transfers.

The taxability of membership dues or annual fees charged by trade groups or associations shall depend on whether or not such payments clearly constitute compensation for asset transfers provided by the respective trade group or association. When such a correlation is not clear, payments shall not be taxable if the trade group or association concerned does not consistently treat such payments as compensation for asset transfers and if the enterprises that are members of the organization do not recognize such payments as taxable purchases.

The transactions listed below are treated as transactions made for compensation.

- (a) Asset transfers made as payment in substitute;
 - (b) Asset transfers made as a substantial gift;
 - (c) Capital contribution of assets other than cash (excluding succession according to special law);
 - (d) Successions of loans and other monetary claims (excluding general successions); and
 - (e) Transmission of wireless communications for the purpose of direct reception by a number of unspecified persons per a law requiring the receiving persons to enter into a uniform contract for such reception and charging fees as prescribed in the contract.
- (4) Sales and leasing of assets or provision of services
- (a) Sales of assets

Sales of assets means transfers to third parties of assets without modifying their identity and without regard to the mode of these transfers. As such, they also include transfers of assets made for the fulfillment of guarantee obligations owed on behalf of third parties or the realization of assets made per procedures for compulsory conversions. Similarly, transfers of ownership or other rights on land made per the procedures prescribed in the Land Expropriation Law or other laws with compensation for the loss of rights paid by the parties acquiring such rights are included in the sales of assets effected for compensation.

- (b) Leasing of assets

Leasing of assets includes any and all acts made for the creation of rights

pertaining to assets and permitting their use by other parties.

“Creation of rights pertaining to assets” means the creation of surface rights or easements pertaining to land, granting the right of expropriation, or a license for industrial property rights (including patent rights, utility model patents, design rights and the right of trademark) and the creation of copyrights pertaining to authors’ works.

“Any and all acts permitting the use of assets by other parties” include, for example, the following:

- ① Use or deposit of industrial property rights;
 - ② Reproduction, performance, and broadcasting of authors’ works or any other acts permitting their exploitation and;
 - ③ Provision of know-how.
- (c) Provision of services

Provision of services means the rendering of services such as civil engineering and construction work, repair, transportation, safe custody, printing, advertisement, brokerage, entertainment, technical assistance, provision of information, stage performance, and writing. It also includes services rendered by lawyers, certified public accountants, certified tax accountants, writers, athletes, movie directors, and professional *go* or *shogi* players, drawing on their professional knowledge or skills.

3. Criteria for Classification of Domestic and Overseas Transactions

a. Sales or leasing of assets

The classification of domestic and overseas transactions is based on whether the assets sold or leased are physically located in Japan at the time of the transaction.

As for the following asset categories, however, classification is based on whether the relevant entities or places are located in Japan at the time of sale or lease.

(1) Ships (limited to registered vessels)

Classification depends on the location of the official agency which registers the ship. In cases where the ship was registered in more than two countries, classification depends on the location of the official agency which registers the ship. In cases where non-Japanese ships are transferred or leased by residents and where Japanese ships are transferred or leased by nonresidents, the residence, main office, or principal place of business of the lessor determines classification.

(2) Ships other than those covered by (1) above

Classification depends on the location of the office, place of business, or

similar facility of the seller or the lessor where the business of the sale or leasing is conducted.

(3) Aircraft

Classification depends on the location of the official agency which registers the aircraft. In cases where the aircraft is not registered, the office of the seller or the lessor where the business of sale or leasing is conducted determines classification.

(4) Mining rights or mine lease rights, stone-quarrying rights, and other rights for the quarrying or excavation of earth and rocks, mining concession areas, mine lease areas, or stone quarrying areas covered by quarrying or excavation rights determine the classification.

(5) Patent rights, utility model rights, design rights, rights of trademark, rights of circuit layings and use rights (including rights for exploitation); the location of the official agency that registers these rights determines classification. In cases where there are registrations of the same right in two or more countries, the place of the seller's residence determines classification.

(6) Copyrights (including publishing rights, quasi-copyrights, and other rights of a similar nature) or production formulas using special technology or others of similar nature (know-how); the place of abode of the seller or lessor.

(7) Goodwill, fishing rights, or right of entry into a fishing ground; the place of abode of business entities doing business in connection with those rights.

(8) Assets shown in (a) through (f) below; the place shown correspondingly for each item.

(a) Securities (securities provided for in Clause 1, Article 2 of the Securities Transaction Law (excluding shares of golf club memberships)); the place where the securities are situated.

(b) Registered national government bonds and other bonds (national government bonds, local government bonds, and corporate bonds (including bonds issued under special laws by juridical persons other than corporations) registered under the provision of the Law Concerning National Government Bonds and the Corporate Bond Registration Law and foreign bonds of a similar nature) and foreign bonds of a similar nature); the place where the official agency that registers these bonds is situated.

(c) Equity interest of investors in corporations; the place where the main office or the principal place of business of the corporation concerned is situated.

(d) Mortgage securities; the place where the mortgage securities are situated.

Consumption Tax

- (e) Loans, deposits, accounts receivable and other monetary claims (excluding those shown in (f) below and including monetary claims pertaining to negotiable certificates of deposit and commercial papers); the place where the office of the creditor concerned conducting the sale is situated.
- (f) Shares of golf club memberships and monetary claims pertaining to deposits with golf clubs or other sports clubs; the place where the golf club or other sports club is situated.
- (9) Assets other than those listed in (1) through (8) above without any clear indication where they are situated; the office where the entity engaging in the sale or leasing of these assets conducts such business.

b. Provision of Services

Classification of domestic and foreign transactions is based on whether or not the service in question is provided in Japan.

As for the following service categories, however, classification is based on whether or not the places shown below are situated in Japan at the time the service is provided.

- (1) Transportation of passengers or cargoes conducted within and outside Japan; the place of departure, shipment, destinations of the passengers, or cargoes.
- (2) Communications conducted within Japan and internationally; the place of dispatch or reception.
- (3) Mail services conducted within Japan and internationally, etc.; Place of forwarding or delivery.
- (4) Insurance; Place where the office of the entity (engaged in the business of insurance excluding those who act as agents in the conclusion of insurance contracts) concluding insurance contracts is situated.
- (5) Provision or design of data; the place where the office of the entity engaged in the provision or design of data conducts such business is situated.
- (6) Provision of services pertaining to research, planning, projection, consultation, supervision, or examination requiring professional knowledge in specialized fields of science and technology made in connection with the construction or production of manufacturing facilities; the place where most of the materials needed for the construction or production of the manufacturing facilities are procured.

In this context, manufacturing facilities shall mean the following items:

- (a) Buildings (including attached facilities) or structures;
- (b) Facilities for mining and manufacturing production, electric power generation and transmission, railways, roads, port facilities, and other transportation services or fishery production;

- (c) Facilities for the transformation and distribution of electrical current, the storage and supply of gas, the storage of oil, communications and broadcasting, water service for industrial use, water supply and sewerage systems, waste water disposal stations (including facilities of a similar nature), agricultural productions and forestry production and;
- (d) Ships, railway vehicles and aircrafts.
- (7) Provision of services other than those listed in (1) through (6) above, conducted within Japan and internationally without any clear indication as to where they have been provided; the place where the office of those entities engaged in the provision of such services is situated.
- c. Financial transactions**

For the lending of money with interest as compensation (including the acquisition of national government bonds and other bonds for interest as compensation and the holding for special drawing rights provided for in the Agreement of the International Monetary Fund) and other acts stated below, classification of domestic and foreign transactions shall be based on whether or not the office of the entity concluding these acts is situated in Japan.

 - (1) Placing of deposits or savings;
 - (2) Placing of money in trust for collective management, including jointly managed trusts and investment trusts that aim dividends from revenue as compensation;
 - (3) Payment of mutual installments as compensation or installments of fixed period savings;
 - (4) Payment of installments to mutual aid credit contracts;
 - (5) Obtaining mortgage securities for interest as compensation;
 - (6) Acquisition of national government bonds and other bonds for profits from redemption as compensation;
 - (7) Discounting of notes and;
 - (8) Receipt of, or other succession to, monetary claims (not including cases of general succession).

4. Non-taxable Transactions

The following transactions are exempt from taxation:

a. Sales and leasing of land

Sales and leasing of land (including establishment, sales, and leasing of rights relating to land); the rights relating to land including superficialities, easements, perpetual tenancy rights, and other rights relating to the use of and benefiting from land, except for mining rights and hot springs usage rights.

Land leased for a period shorter than one month and used in conjunction

Consumption Tax

with buildings, parking lots, and other facilities are taxable.

b. Sales of securities and means of payment

Sales of securities such as national government bonds, corporate bonds, and stocks (excluding shares of golf club memberships); sales of registered bonds, ownership, or membership shares of partnership and cooperative associations and monetary claims certificates of deposits.

Sales of means of payment (excluding those for collection or sale) and provision of money-changing services.

c. Money lending and other financial transactions

The lending of money for interest as compensation, provision of such services as guarantees, provision of services effected, as compensation, for trustee remuneration from jointly managed money trusts or bond investment trusts, insurance premiums (excluding fees received separately as administrative expenses), and other similar services (such as sales of assets for compensation for specified interest, and insurance premiums for financial leasing, installment sales fees, and mutual-aid installments).

d. Sales of postal and other stamps

Sales of postal and other stamps (provided sales are made at designated places) and similar items.

e. Sales of certificates for the provision of goods and services

Sales of certificates for the provision of goods and services (such as “telephone cards”).

f. Registration and licensing fees by the national government and local public bodies

Provision by the national government and local public bodies of services related to registration, licensing, passport control, resident and family certification, and certain other similar services.

g. Services such as international postal money transfers

h. Medical services, etc. in the public medical care systems

Medical services (including payment of medical benefits) made under medical insurance laws, such as the Health Insurance Act, the Elderly Health Protection Act, the Livelihood Protection Law, the Law Concerning Compensation for Ill Health caused by Environmental Pollution, the Workers Accident Compensation Act, and other similar medical services, and medical treatment given to the victim related to indemnity under the Automobile Accident Compensation Security Act (up to a certain limit with respect to payment for special hospital rooms).

i. Nursing Care Services specified services provided under the Nursing Care Insurance Law

j. Social Welfare Services

Social Welfare Services defined under the Social Welfare Services Act (including relevant rehabilitation and relief services defined under the Rehabilitation and Emergency Relief Act; excluding sales and leasing of assets or provision of services by industrial training institutes).

- k.** Transfer of assets, etc., conducted by businesses similar to social welfare services, such as meal delivery services for the elderly, etc.
- l.** Delivery of babies (including delivery not covered by medical insurance laws under medical insurance laws)
- m.** Burial and crematory services
- n.** Transfer or lease of equipment with special properties, structures, or functions for the physically handicapped
- o.** Educational services

Services effected as compensation for tuition, entrance fees, entrance examination fees, facility charges, and certification fees for schools defined under Article 1 of the School Education Act, special schools under Article 82 (2) of the same law, vocational schools under Article 83 of the same law (provided that the course of study lasts more than a year), and other kinds of schools specified in Articles 1, 82 (2) and 83 of the same law.

- p.** Transfers of textbooks defined in the School Education Act
- q.** Housing rent

Note: Transactions mentioned at above k, l, m, n, p, q, and in some parts of j and o have been exempt from taxation since 1 October 1991.

5. Tax Exemption for Exports, etc.

In principle, consumption tax seeks to impose tax on goods and services in the country where they are consumed (principle of taxation at consumption places). Therefore, transfer of taxable assets that taxable business operators engage in trades, similar to export trading and international transportation, is exempt from consumption taxation.

In addition, according to international practice, transfer of taxable assets to embassies and other diplomatic missions of foreign governments are exempt from consumption tax taxation.

Tax exemptions are differentiated from non-taxable transactions in that the consumption tax levied on purchases made for tax-exempt transactions is deductible.

a. Tax exemption for exports

(1) Scope of exemption

Export transactions qualifying for exemption are taxable asset transfers effected within Japan and specified as follows:

Consumption Tax

- (a) Sales or leasing of assets effected as exports from Japan

This category applies exclusively to enterprises directly involved in export transactions. It does not apply to enterprises subcontracted for the processing of goods manufactured for export and those selling export items to enterprises engaged in export transactions.

- (b) Sales and leasing of foreign cargoes

Foreign cargoes are those for which export licenses have been obtained and cargoes arriving from foreign countries (including marine products collected or caught by foreign ships operating on the high seas) for which import licenses have not been obtained.

- (c) Transportation of passengers or cargoes, communications and mail services conducted within Japan and internationally

International transportation, communications and mail services are regarded as export transactions.

- (d) Repair work on ocean liners done at the request of ship operators or leasers.

- (e) Sales or leasing of ship and aircraft and ship for the transportation of passengers or cargoes exclusively between destinations within and outside Japan, or between destinations outside Japan (aircraft operating in international routes) for air transportation enterprises, etc.

- (f) Repair work on aircraft operating in international routes done at the request of air transportation enterprises, etc.

- (g) Sales or leasing of containers used for the transportation of cargoes between destinations within and outside Japan or between destinations outside Japan, to ship operators lease ship or air transporters (ship operation business enterprises, etc.), or repair work on containers done at the request of ship operation enterprises, etc..

- (h) Supplies of services to ship operation enterprises, etc., such as pilotage and other assistance in the entry or landing and departure of ocean liners or aircraft operating in international routes, or facilities for the entry or landing and departure, anchorage or parking of ocean liners, etc., and other similar services.

- (i) Supplies of services related to foreign cargoes such as stevedoring, transportation, custody, tallying, surveying, and other similar services.

These supplies of services further include those related to cargoes kept in “designated bonded areas”, bonded warehouse, bonded exhibiting areas, and bonded comprehensive areas for the purpose of export, and cargoes kept in these places for which import licenses have been obtained. With regard to the supplies of these services related to the specified export cargos, exemption is limited to the supplies conducted at the

“designated bonded area” or at the places where such cargoes are embarked on ships or aircrafts. Furthermore, “supplies of other similar services” related to foreign cargoes include, for example, tallies on foreign cargoes, services related to harbor transportation customs clearance of imported cargoes, and fumigation of vegetables and fruits.

- (j) Sales and leasing to nonresidents of mining rights, mine lease rights, stone-quarrying rights, and other rights for the quarrying and excavation of earth and rocks, industrial property rights (patent rights, utility model patents, design rights, and trademark rights) or circuit laying and use rights (including right to the use of these rights), copyrights (including publishing rights, quasi-copyrights, and similar rights), production formulas using special technology and others of a similar nature (know how), franchise rights, fishery rights, or right of entry into fishing grounds.
- (k) In addition, the provision of services to nonresidents, except for:
 - (a) Transportation or custody of assets situated in Japan;
 - (b) Services related to food, drinking, and lodging in Japan; and
 - (c) Services similar to (a) and (b) above and directly provided in Japan.

b. Tax exemption for sales of export goods at export goods sales facilities

Sales of goods (exports for daily life) by enterprises operating export goods sales facilities for nonresidents, such as foreign travelers and U.S. military personnel stationed in Japan, are exempt from consumption tax by fulfilling certain procedures.

c. Tax exemption for sales of goods loaded on ocean liners, etc.

The tax exemption for export transactions in (1) above applies to the loading of Japanese goods on ships or aircraft registered in foreign countries (domestic registered ships, etc.) while the tax exemption for the loading of goods for use aboard ships or aircraft applies to the receipt of delivery from bonded areas of goods for use aboard ships or aircraft for loading in foreign registered ships, etc. For an equitable balance, the same exemption is afforded to the loading of goods for use aboard Japanese ships or aircraft.

d. Tax exemption for sales of taxable assets to foreign embassies and other diplomatic missions

Sales of taxable assets by enterprises designated by the Director General of the National Tax Agency to foreign embassies, legations, consulates, or other similar diplomatic missions or to foreign ambassadors, ministers, consuls, or other similar diplomatic representatives are exempt from consumption tax, provided that such sales have been effected with the embassies, etc., or the ambassadors, etc., by presenting documents in prescribed form certifying that the taxable assets in question are necessary for the performance of their diplomatic, consulate, and other missions, with attached papers showing the

Consumption Tax

particulars of the purchases in prescribed form.

As part of the principle of reciprocity, however, this exemption shall be restricted for embassies, or ambassadors, etc., representing countries that restrict exemption from taxes similar in nature to consumption tax for Japanese embassies, etc., in these countries, or Japanese ambassadors, etc., accredited in these countries.

To qualify for this exemption, the designated enterprises are required to keep papers submitted by the embassies, etc., or the ambassadors, etc., in good order and maintain their files at the place of tax payment or at their offices that conducted the asset transfers in question for seven years after the time limit for filing final tax returns.

With the exception of unavoidable circumstances, the embassies, or ambassadors, etc., may not use the assets in question for purposes other than the performance of their missions for two years after the application of this tax exemption.

- e. Tax exemption for the sale of goods to shopping facilities operated by the U.S. Navy.

Sales by enterprises to shopping facilities operated by the U.S. Navy or PXes, of goods purchased by members or civilian employees of the U.S. armed forces or their families (members of the U.S. armed forces) for the purpose of export and that follow prescribed procedures are exempt from consumption tax.

The prescribed procedure mentioned above requires that U.S. armed forces members, at the time of purchase, submit papers to the shopping facilities (operated by the U.S. Navy or PX) with entries noting that the purchase in question is for the purpose of export in exchange for delivery of the purchased items.

The scope of goods eligible for this tax exemption is the same as that for goods eligible for tax-exempt sales at export goods sales facilities in b. above.

6. Import Transactions

- a. Taxable Foreign Cargoes

- (1) Transfers of cargoes without compensation

Foreign cargoes received from bonded areas are subject to taxation even if their receipt involves no payment of compensation. In domestic transactions, however, transfers of cargoes effected without compensation are not subject to taxation. Imports are, in effect purchases for consumption in Japan, and taxation on the receipt of cargoes without compensation is necessary to keep the tax burden balanced between domestic and foreign products.

(2) Receipt of delivery from bonded areas

Cargoes such as mail received from bonded areas are regarded as having been received from bonded areas and, as such, are subject to taxation.

(3) Consumption or use inside bonded areas

Consumption or use of foreign cargoes inside bonded areas (designated bonded areas, bonded storehouses, bonded factories, bonded exhibiting areas, and comprehensive bonded areas) is also regarded as receipt of delivery from bonded areas and, as such, is subject to taxation. In cases where foreign cargoes are consumed or used as raw materials for the manufacture of taxable goods, such consumption or use is not subject to taxation.

In cases where goods are received from bonded areas for domestic consumption or use instead of being re-exported to foreign countries, such products are subject to taxation based on their delivery price at the time of the import declaration.

Consumption or use of sample tests of foreign cargoes extracted by customs officials under the Customs Act, or those taken into custody by authorized officials of public agencies under the provisions of other relevant laws and regulations are excluded from taxation.

b. Tax-Free Foreign Cargoes

Foreign cargoes excluded or exempt from taxation are: Securities, postage stamps, revenue stamps, certificate stamps, and commodity stamps, certain kinds of equipment for the physically handicapped, and certain kinds of textbooks are exempt from taxation;

c. Tax-Exempt Foreign Cargoes

Excluded or exempt from taxation are accorded foreign cargoes such as:

- (1) Foreign cargoes amounting to less than ¥10,000 in total taxable value are, in principle, exempt from taxation;
- (2) Ocean liners imported by enterprises engaged in ship operations are exempt from taxation and;
- (3) Cargoes for use by diplomats are exempt from taxation.

8/3 Taxpayers

1. General

Taxpayers are defined as enterprises and those who receive foreign goods from bonded areas.

In other words, taxpayers in domestic transactions are limited to enterprises, including individual proprietors. In contrast, consumers can become taxpayers when they receive taxable cargoes from bonded areas.

Consumption Tax

Enterprises include individual proprietors and corporations. In this context, however, organizations without juridical personality, such as unincorporated associations and foundations with officers designated as representatives or administrators, are regarded as corporations and, as such, are subject to the provisions of the consumption tax. Small enterprises with taxable sales during the base period of no more than ¥10 million are exempt from tax liability on sales of taxable assets during a tax period. However, this does not apply if there is no tax base for the taxation period, and an exception is established for a corporation whose capital is ¥10 million or more at the time of commencing its taxation period. With regard to the level of the tax exemption system, taxable sales had been set at ¥30 million since the introduction of consumption tax. However, this exemption level was reduced to ¥10 million at the time of the revision in 2003, applicable to the taxation period beginning on April 1, 2004.

2. Base Period

a. Definition of “base period”

The “base period” is the period that determines the existence or absence of tax liability. For individual proprietors, it is the calendar year two years before the current tax year. For corporations with an accounting period of one year, it is the period two years before the current accounting period.

b. Taxable sales during the base period

The taxable sales during the base period is the amount obtained by deducting the total sum of refunded sale prices, not including tax, (amounts for returned goods unsold, deductions, or rebates) from the total sum of prices (not including the consumption tax) received as compensation for the transfer of taxable assets effected within Japan during the base period.

In cases where a corporation’s base period is not one year, the taxable sales during the base period is the amount obtained by prorating the balance after deducting the total sum of refunded sales prices, not including tax, from the total sum of prices received as compensation for the transfer, etc. of taxable assets during the above-mentioned base period. The proration is made by first dividing the above balance by the total number of months in the accounting period included in the base period and multiplying the result by 12.

These calculations are to include sales in export transactions exempted from the consumption tax and the amount returned from the compensation received in export transactions.

3. Election of Non-Exemption from Tax Liability

Under consumption tax law, deductions of various kinds, including deductions

for amounts paid as a consumption tax on purchases are, as detailed later applicable only to taxpayers. Therefore, enterprises primarily engaged in export transactions, with taxable sales amounting to less than ¥10 million for the base period, can elect to forego tax liability exemption to qualify under certain procedure, as taxpayers, for deduction or refund of the amount paid as consumption tax on their purchases.

4. Special Rules in Cases of Inheritance, Corporate Mergers, and Corporate Division, etc.

a. Inheritance

- (1) In cases where an inheritance takes place during the current year, and the successor's taxable sales amount to less than ¥10 million for the corresponding base period, if the business of the ancestor has total taxable sales more than ¥10 million for the said base period, there is no tax liability exemption for the transfer of taxable assets by the successor during the period from the day after the inheritance to 31 December of the same year.
- (2) In cases where the successor of an inheritance that took place two years before the current year has taxable sales amounting to no more than ¥10 million for the base period corresponding to the current year and the total of these taxable sales by the successor in question for said base period and the taxable sales by the ancestor for the same base period exceed ¥10 million, there is no tax liability exemption for the transfers, etc. of taxable assets by the successor during the year.

In the case of an inheritance by two or more successors of business establishments operated by the ancestor at two or more places of business, and where each place of business has been apportioned to one of the successors, the taxable sales by the ancestor for the base period are to be calculated as amounts generated at each succeeded place of business.

In cases where the inheritance of the ancestor's business establishment has taken place during the three years preceding the current year, tax liability is determined by the total taxable sales by the ancestor in question during the base period and the taxable sales by the successors during the same base period.

b. Corporate mergers

- (1) Mergers
 - (a) Determination of tax liability for the accounting period during which mergers took place

In cases where mergers took place during the current accounting period and the transferee corporations with taxable sales amounted to no

more than ¥10 million for the base period corresponding to the current accounting period succeeded to the business of the amalgamated corporations with taxable sales exceeding ¥10 million for the base period, there shall be no tax liability exemption relating to the transfer, etc. of the taxable asset during the period from the day of the said merger to the end of the current accounting period.

- (b) Determination of tax liability in case where mergers took place after the start of the base period

If mergers took place during the period from the second day of the base period corresponding to the current accounting period to the day prior to the current accounting period and if the sum of taxable sales by transferee corporations for the base period and of taxable sales by the amalgamated corporations for the period corresponding to the said base period exceed ¥10 million, there shall be no tax liability exemption during the current accounting period (limited to cases where taxable sales for the base period are no more than ¥10 million).

- (2) Incorporation by merger

- (a) Determination of tax liability for the accounting period during which an incorporation by merger took place

In case where a corporation was established by merger and one of the amalgamated corporations has taxable sales exceeding ¥10 million for the base period corresponding to the accounting period in which the day of the said merger fell, there shall be no liability exemption for transfer, etc. of taxable assets by the corporation established by the merger during the accounting period in which the day of the said merger fell.

- (b) Determination of tax liability in cases where incorporation by merger took place after the start of the base period

If mergers took place during a period from the day two years before the first day of the current accounting period to the day before the first day of the current accounting period and if the sum of taxable sales by transferee corporations during the said period and of taxable sales by amalgamated corporations for the period corresponding to the base period of transferee corporations exceed ¥10 million, there shall be no tax liability exemption for transfers of taxable assets by the transferee corporations for the accounting period (limited to cases where taxable sales of transferee corporations for base period no more than ¥10 million).

- c.** Corporate divisions, etc.

- (1) Scope of divisions, etc.

The scope of divisions covers corporations established through investment in kind and so-called irregular investment in kind (postmortem in-

corporation) in addition to divisions under the Corporate Code (division for incorporation, division for absorption). We define that “division” is a reorganization form where a new corporation succeeds to the existing business while “division for absorption” is a reorganization form where the existing corporation succeeds to the business.

(a) Divisions, etc.

1. Division for incorporation

Corporations stipulated in the Corporate Code

2. Incorporation in certain investment in kind

This is a corporation whose total of outstanding shares is owned by the investing company or whose total of capital is subscribed by the investing company.

3. Postmortem incorporation

When a corporation incorporates a new corporation with money contributed to set up another corporation and when the founding corporation transfers the assets of the corporation incorporated to a third party after the incorporation based on a “postmortem incorporation” contract stipulated in the Corporate Code or the Private Limited Company Law, the founded corporation that meets the requirements stated below falls into postmortem incorporation.

a) The total of outstanding shares of or the total of capital of the founded corporation is owned by the investing company (the equity is wholly owned) at the time of incorporation

b) Transfer of the assets of the founded corporation is scheduled at the time of incorporation and when the transfer is executed within the six months after the incorporation

(b) Division for absorption

Divisions stipulated in the Corporate Code

(2) Method for concrete determination of tax liability

(a) Case of divisions

1. Determination of tax liability of divided subsidiary corporations (corporations formed through division)

a) Accounting period that includes the day of the division (first accounting period)

When taxable sales of the parent corporation within the period corresponding to the base period of the accounting period of a divided and newly established subsidiary corporation (any of the parent corporations if they are two or more) exceeds ¥10 million, there shall be no tax liability exemption.

b) When a division takes place within the period one day before the

year prior to the start day of the accounting period until one day prior to the start day of the accounting period (second accounting period of one-year settlement corporation)

When taxable sales of the parent corporation (any one of the parent corporations if the parent companies are two or more) for the period corresponding to the base period of the accounting period of the divided subsidiary company exceed ¥10 million, there shall be no tax exemption.

- c) When divisions took place before at least one year and two days prior to the start day of the accounting period (not including the case where there are two or more parent corporations) (third accounting period or later of one-year settlement corporations)

If taxable sales of the corporation for the base period of the accounting period is no more than ¥10 million and if the divided subsidiary satisfies specific requirements at the last day of the base period concerned with the accounting period and if the sum of taxable sales of the subsidiary for the base period of the accounting period and of taxable sales of the parent corporation exceeds ¥10 million, there shall be no tax liability.

※The specific requirements are as follows:

The total of outstanding shares of a subsidiary or more than 50/100 of capital of a subsidiary is owned by the parent corporation and a person who has special relationship with the parent corporation.

2. Determination of tax liability of a dividing parent corporation (corporation who had divisions)

- a) Accounting period that divisions took place and the following accounting period

Tax liability shall be determined by taxable sales of the parent corporation for the base period.

- b) When divisions took place at least one year and two days prior to the start day of the accounting period (third accounting period or later of one-year settlement corporations after divisions)

If taxable sales of the parent corporation for the base period of the accounting period is no more than ¥10 million and if the divided subsidiary satisfies specific requirements at the last day of the base period concerned of the accounting period and if the sum of taxable sales of the parent corporation for the base period of the accounting period and of taxable sales of the subsidiary for the period corresponding to the base period exceeds ¥10 million, there shall be no tax exemption.

(b) Case of division for absorption

1. Determination of tax liability of a divided and succeeding corporation (corporation that succeeds to the business of the divided corporation)

a) Accounting period within which a division took place for absorption (accounting period that the division took place)

If taxable sales of a succeeding corporation for the base period of the accounting period within which the division took place for absorption is no more than ¥10 million and if taxable sales of the divided corporation (taxable sales of any one of the divided corporations if they are two or more) for the period corresponding to the base period exceed ¥10 million, there shall be no tax exemption.

b) When a division took place for absorption within the period from one year and one day prior to the start day of the accounting period until one day prior to the start day of the accounting period (accounting period following the accounting period that the division took place)

If taxable sales of the dividing corporation is no more than ¥10 million for the base period of the accounting period and if taxable sales of the divided corporation (taxable sales of any one of the divided corporations if they are two or more) exceed ¥10 million, there shall be no tax exemption.

c) When a division took place within the period of at least one year and two days prior to the start day of the accounting period (third accounting period or later of one-year settlement corporations)

Determination of tax liability depends on taxable sales of the divided and succeeding corporation for the base period.

2. Determination of tax liability of the dividing corporation (corporation that divided itself)

Determination of tax liability depends on the taxable sales of the dividing corporation for the base period.

8/4 Place of Tax Payment

a. Place of tax payment for domestic transactions

- (1) Individual proprietors – ① if they have domiciles in Japan, the place of payment is the location of the domicile; ② in cases where they have dwellings instead of domiciles, the location of the dwellings; and ③ in cases where they have neither domiciles nor dwellings but have offices in Japan, the location of the office.
- (2) Corporations – ① for domestic corporations, the location of their main

Consumption Tax

office or principal place of business; and ② for foreign corporations with offices in Japan, the location of the office.

b. Place of tax payment for import transactions

The place of payment for foreign cargoes received from bonded areas is the location of the bonded area.

8/5 Attribution of Asset Transfers, etc.

- a.** In asset transfers, etc. those who substantially enjoy compensation are regarded as entities who have effected asset transfers, etc.
- b.** In the case of assets belonging to trust properties, their transfers are regarded, in principle, as having been effected by the beneficiaries.

8/6 Time of Asset Transfers, etc.

1. General Rules

The realization of tax liability for domestic transactions is at the time of transfer of taxable assets, etc.

a. Time of inventory sales

Sales of inventory are regarded as having been effected on the day of delivery. The day of delivery is the day that an enterprise concerned has consistently chosen for sales out of all days that can be reasonably regarded for delivery, based on the type and quality of the inventory as well as the contents of the sales agreement, such as the day of shipment; day of receipt upon inspection by the counterparty; the day on which the inventory sold becomes available for beneficial use by the counterparty; and the day on which the volume of sales has been confirmed by methods such as a meter check.

If forests or wilderness areas constitute the inventory and the day of delivery is not clear, delivery is regarded as having been made either on the day on which payment of approximately 50 percent or more of the sales price has been received or on the day on which an application has been submitted for registration of the transfer of ownership, whichever is earlier.

b. Time of asset transfers by contract

The time of asset transfers by contract is, in principle, for a contract requiring delivery of goods by the day on which all of the objects of the contract have been completed and, when delivered to the counterparty for a contract not requiring delivery of goods, the day on which contracted services have been fully provided.

c. Time of transfer of fixed assets

The time of transfer of fixed assets is, in principle, the day of delivery. In cases where the fixed assets consist of land, buildings, or other similar assets, the time of their sale can be the day the sales agreement takes effect.

d. Time of asset transfers, etc. in return for rent payments as compensation

The time of asset transfers, etc. in return for the payment of rent as compensation (excluding amounts received in advance) based on lease agreements is the day on which rent comes due in accordance with the agreement or business customs.

2. Exceptions for Time of Asset Transfers for Installment Sales

a. Tax period during which installment sales took place

In cases where assets (inventory in the case of individual proprietors) have been sold or transferred on a deferred payment basis, or where asset transfers have been effected in construction work (including manufacture and excluding long-term, large-scale construction work) or other supplies of services contracted on a deferred payment basis and where the amount of compensation for such sales or transfers are to be recognized by way of a deferred payment basis, portions of such assets or the objects of such contracts for which installments have not yet come due during the tax period that includes the day of such sales (excluding amounts received during that tax period) are regarded as not having been sold or transferred during that tax period and the amount of compensation for the portions for which installments have not yet come due may be deducted from the amount of compensation for such assets or the object of the contract.

b. Tax periods after the tax period during which sales on a deferred payment basis took place

During the next tax period and each subsequent tax period following the period during which installment sales took place, asset transfers are regarded as having taken place during the respective tax period corresponding to installments coming due (excluding amounts received as installments before the first day of that tax period and including amounts coming due after the last day but received during that tax period).

3. Exception for Time of Asset Transfers for Construction Work

a. Long-term, large-scale construction work

In cases where asset transfers are effected based on long-term contracts for construction work on a large-scale and where the amount of compensation is calculated by the percentage of completion method, asset transfers for the

Consumption Tax

portions corresponding to compensation calculated in a tax period can be treated as having been effected during that tax period.

b. Construction Work

In cases where asset transfers are effected on contracts for construction work (excluding long-term, large-scale construction projects of great size) and the amount of compensation for such transfers (excluding those showing losses) are to be recognized by the percentage of completion method, assets transferred for the portion corresponding to compensation calculated in a tax period can be treated as having been effected during that tax period.

c. Tax period during which the delivery was made

In cases where construction work (including long-term, large-scale construction work of great size) was completed and delivered, the amount of compensation for the portion for asset transfers deemed effected before the period during which the delivery was made may be deducted from the amount of compensation for such asset transfers.

8/7 Tax Base and Tax Rate

1. Tax Base

a. Tax base for domestic transactions

The tax base for domestic transactions is the amount of compensation for the transfer, etc. of taxable assets, etc.

The amount of compensation for the transfer of taxable assets is the amount of all money, goods other than money, rights, or other economic benefits received or to be received as compensation for the transfer of taxable assets, not including amounts equal to those paid as consumption tax and local consumption tax.

In this context, the term “amounts to be received” does not, in principle, mean the market value of the transferred assets, but rather such amounts that have been agreed upon between the parties.

In addition, goods other than money, rights, or other economic benefits include arrangements that substantially produce the same economic results as the receipt of consideration for transfer of assets, such as the delivery of goods other than money or rights, or the lending of money free of charge or at rates lower than current market rates as essentially compensation for the transfer of taxable assets, etc.

(1) Amount of compensation for special forms of transfer of taxable assets, etc.

(a) Payment in substitute

The amount of compensation for asset transfers, etc. made as payment in substitute is the amount equal to liabilities eliminated by the payment in substitute.

(b) Substantial gift

The amount of compensation for asset transfers, etc. made as substantial gift is the amount equal to the value of the accompanying liabilities.

(c) Investment in kind

The amount of compensation for asset transfers, etc. made as investment in kind is the amount equal to the value of the shares (including investment certificates) acquired in return for investment at the time of acquisition.

(d) Exchange

The amount of compensation for asset transfers, etc. made in the form of exchange is the amount equal to the value of the assets acquired in exchange at the time of acquisition.

In case where margins of exchange are paid and received, the receiving party shall add amounts received as margin to the value of the assets acquired by exchange, while the paying party shall deduct amounts paid as margin from the value of the assets acquired by exchange.

(2) Calculation of compensation amount

(a) Division of the amount of compensation for co-mingled sales of taxable and non-taxable assets

In cases where taxable assets and non-taxable assets have been sold together for one price without respectively marking the amounts of their compensation, the price must be divided into components in a reasonable way. If no reasonable method is available, the division is to be made in proportion to the respective market values of the taxable and non-taxable assets.

(b) Money or other valuables received for the payment of stamp tax, etc.

In cases where money, etc. received by enterprises as compensation for the transfer of taxable assets, etc. include amounts equal to the value of stamp duties and other charges owed, in principle, by the enterprises to the national government or local public bodies, such amounts for the payment of stamp duties and other charges may not be deducted from the amount of compensation for the transfer of taxable assets.

Meanwhile, registration and license tax, automobile tonnage tax, automobile acquisition tax, other transaction taxes, and public charges owed, in principle, by entities who receive transfers, etc. of taxable assets

Consumption Tax

shall not be included in the amounts of transfers of taxable assets for compensation so far as that effect is clearly stated in bills, etc.

(c) Treatment of specific indirect taxes

Amounts of compensation for the transfer of taxable assets, etc. should include the liquor tax, tobacco tax, gasoline tax, and LPG tax, etc. However, since the taxpayers for the light oil delivery tax, golf course utilization tax, and bathing tax are consumers, these taxes should not be included in the amount of compensation in cases where such amounts are clearly marked.

(d) Treatment of returned unsold goods and discounts, etc.

In cases where returned unsold goods, discounts, or rebates take place in connection with the transfer of taxable assets, etc. exclusion of the amount of returned or unsold goods, discounts, or rebates from the sales figures and recognition of the balance as the amount of compensation is permitted on condition of consistent application of the same principle.

(e) Value of self-consumption

In cases where individual proprietors use their assets for self consumption or corporations transfer their assets to their directors as gifts, or at extraordinarily low prices, the amount of compensation is determined on the basis of the market value of the assets so used or transferred.

However, in cases where individual proprietors use their inventories for self-consumption or corporations transfer their inventories to their directors as gifts and they declare in their final tax returns amounts larger than the compensation actually paid for the taxable purchases of such inventories as the amounts of compensation for assets used for self consumption, and larger than approximately 50 percent of the normal sales price of those inventories the declared amounts are acceptable.

b. Tax base of consumption tax for import transactions

The tax base for import transactions is the delivery price (including customs duties and other selective consumption taxes) of imported goods.

2. Tax Rate

The current tax rate is 4% (and 1% Local Consumption Tax, a local tax, was also introduced with the current rate for a total of 5%).

The tax rate was raised from 3% on 1 April 1997.

8/8 Tax Credit for Consumption Tax on Purchases, etc.

1. Tax Credit for Consumption Tax on Purchases

Concerning taxable purchases made by enterprises in their country or taxable cargoes received from bonded areas, the consumption tax arising on taxable purchases in the said taxable period and the consumption tax imposed or to be imposed on taxable cargoes that are received from bonded areas may be deducted from the consumption tax to the tax base (amount of consumption tax on sales) for the taxable period that include the days when the said taxable purchases are made or the days when the deliveries of taxable cargoes from bonded areas are received (which include the period of the days when the special returns are filed for the said taxable cargoes)

a. Qualifying enterprises

- (1) This deduction is only afforded to enterprises with tax liability and not to those exempt from payment.
- (2) This deduction is applicable to the period which includes the days of taxable purchases or receipts for deliveries of taxable cargoes from bonded areas in Japan (in case special returns are filed for taxable cargoes, the period that includes the days when the special returns concerned are filed)

b. Definition of taxable purchases

Taxable purchases means receipt of transfers or the borrowing of assets from other entities or receipt of services provided by other entities, each made as a business activity by business enterprises. Provision of services made in return for the payment of salaries and transfers of non-taxable assets and tax-exempt transfers of assets do not fall under this definition.

Taxable purchases also include, however, purchases by enterprises of taxable assets from tax-exempt enterprises or consumers.

c. Purchases excluded from taxable purchases

Taxable purchases are those made for business purposes. Therefore, those made by individual proprietors for self-consumption do not fall under this category.

Since the provision of services in return for the payment of salaries is not included in this category, directors' compensation, personnel expenses, labour costs, and retirement deductions are not taxable purchases. However, business trip expenses, hotel charges, and other daily deductions that are considered necessary for such trips under normal circumstances, as well as commuting deductions to pay for transportation, all of which are considered necessary for such trips under normal circumstances, are treated as compensation paid in conjunction with taxable purchases.

Consumption Tax

Furthermore, purchases involving transfers of non-taxable assets or taxable assets accorded tax exemption, etc. are not taxable purchases. Therefore, interest paid, ground rent paid, employees' overseas business trip expenses, and international telephone charges do not represent compensation paid in conjunction with taxable purchases.

In addition, since transactions that do not fall under "asset transfers" are, by definition, not included in this category, dividends paid and proceeds from insurance paid are not taxable purchases. Tax credit is only allowed for taxable purchases made in Japan, taxable purchases made outside Japan are not included in this category.

Similarly, of cargoes received from bonded areas, tax credit is not allowed for those afforded tax exemption under other laws or treaties.

d. Calculation of the tax credit amount

(1) Calculation of the tax credit amount

In principle, the entire amount of consumption tax paid on taxable purchases is deductible. However, in order to limit the deduction accorded to purchases involving non-taxable transactions, if the amount of non-taxable sales exceeds 5 percent of total sales during a tax period, the amount deductible as a tax credit on taxable purchases can be calculated either by the itemized method or the proportional method.

Enterprises have the option of choosing either method. In cases where the proportional method is selected, however, it must be used for at least two years.

(a) Itemized method

The amount of tax on taxable purchases during a tax period is divided into tax attributable to taxable sales, etc. tax attributable to the sale of other assets, etc. and tax common to both taxable and other sales. The deductible amount of tax is equal to the sum of ① taxes attributable to taxable sales only and ② taxes common to both taxable and other sales multiplied by the proportion of taxable sales to total sales.

However, the amount of tax common to both taxable and other sales can be allocated between the two by using the predetermined proportion (based on the number of employees, floor space, and similar considerations) approved in advance by directors of the tax offices in lieu of the actual proportion of taxable sales to total sales.

Note:

$$\text{Proportion of taxable sales} = \frac{\text{Amount of compensation for taxable assets sold in the country}}{\text{Total amount of compensation for assets sold in the country}}$$

“Tax attributable only to taxable sales” in (a) above includes, for example, taxable assets sold to third parties without any processing, costs of raw materials, containers, wrapping papers, machinery and equipment, machine tools, other tools, fixtures consumed or used only for the manufacture of taxable assets, and other costs relative to taxable assets such as warehouse charges, freight, advertising expenses, and processing fees. In cases where trial articles and testing products are distributed to customers and other entities concerned as a sales promotion for taxable assets, the amount of tax on taxable purchases of such trial articles and testing products is treated as tax attributable only to the transfer, etc. of taxable assets. Moreover tax attributable only to the transfer, etc. of taxable assets and that qualify for export exemption are included in this category.

In addition, amounts of compensation for the transfer of non-taxable assets made within Japan that constitute export transactions (including interest on loans to nonresidents and foreign bonds) are treated as the amount of compensation for export transactions. And exports of assets for sale outside Japan or self-consumption or use in foreign countries are treated as export transactions.

Note: This treatment does not apply to the export of loans and securities as principal.

“Tax attributable only to the transfer, etc. of other assets” includes, for example, costs for the development of land for sale and purchases of medicine, etc. necessary for medical tests and treatment made under the provisions of the Health Insurance Act.

(b) Proportional method

The amount of deduction is calculated by multiplying the amount of tax on taxable purchases, etc. by the percentage of taxable sales to total sales.

(2) Calculation method for the percentage of taxable sales

Percentage of taxable sales means the weight of the amount of compensation for taxable assets sold within Japan during a tax period in respect to the total amount of compensation for assets transferred within Japan during the tax period.

In the above definition, both the total amount of compensation for assets sold and the total amount of compensation for taxable assets sold do not include the amount of consumption tax. These figures also show the net after deducting the amount of refunded sales prices (due to returned goods unsold, discounts, and rebates). This definition naturally includes amounts of compensation in export transactions but excludes amounts of compen-

Consumption Tax

sation in foreign transactions.

In calculating the percentage of taxable sales, the amount of compensation for transfer of assets, etc. and the amount for transfer of taxable assets, etc. are to include:

- ① Amount of compensation for the sales of non-taxable assets made within Japan constituting export transactions (including interest on loans to nonresidents and foreign bonds) and;
- ② The value of assets (FOB price) exported for sale and self consumption or use outside Japan.

e. Qualifications

To qualify for tax credit on purchases, it is necessary to keep both books and documents as follows for seven years at the place of tax payment or the taxpayers' office:

- (1) Books that record the particulars of taxable purchases and prices and;
- (2) Statements of delivery, bills, etc., or papers issued by customs superintendents that show the particulars of taxable purchases and prices.

2. Adjustment of Tax Deductions on Purchases

a. Adjustment of deduction for refunds of compensation for purchases

(1) Adjustment for refunds of compensation for purchases

In cases where, in conjunction with taxable purchases made within Japan, enterprises receive partial or total return of the compensation paid for such purchases, or have their accounts payable or other liabilities for compensation reduced by returning purchased goods unsold, received discounts, or rebates (refund of purchase prices, etc.), adjustment must be made in the amount of tax on purchases used as the basis for calculation of the deduction for the consumption tax on purchases for a tax period, which includes the day of the refund of purchase prices, etc.

(2) Methods of adjustment

In the case of return of compensation for purchases, etc., the amount of consumption tax on the amounts received as a refund of the purchase price during the tax period (an amount equivalent to $4/105$ of the amount received as a refund of the purchase prices), is deducted from the amount of tax on taxable purchases during the tax period. The methods of calculation are as follows:

(a) In cases where the percentage of taxable sales is 95% or more:

The amount of consumption tax on the amounts received as a refund of purchase prices during the tax period is deducted from the total amount of taxes on the taxable purchases.

- (b) In cases where the percentage of taxable sales is less than 95% and the amount of deduction for consumption tax on purchases is calculated by the itemized method:

① The amount of consumption tax on the amounts received as a refund of the purchase price during a tax period in conjunction with taxable purchases required only for transfers of taxable assets is deducted from the total amount of taxes on taxable purchases required only for transfers of taxable assets during the tax period.

② The amount calculated by multiplying the total amount of the consumption tax on the amounts received as a refund of the purchase price during a tax period in conjunction with taxable purchases required only for the transfer, etc. of both taxable and other assets by the percentage of taxable sales, is deducted from the amount calculated by multiplying the total amount of tax on taxable purchases required for the transfer of both taxable and other assets by the percentage of taxable sales (including percentages similar in nature to the percentage of taxable sales).

- (c) In cases where the percentage of taxable sales is less than 95% and the amount of deduction for the consumption tax is calculated by the proportional method:

Amounts calculated by multiplying the amount of consumption tax on amounts received as return of compensation during a tax period by the percentage of taxable sales are deducted from amounts calculated by multiplying the total amount of taxes on taxable purchases during the tax period by the percentage of taxable sales.

b. Adjustment of deduction for the consumption tax on purchases in other circumstances

- (1) In the case of fixed assets subject to adjustment, the deduction for consumption tax on purchases is adjusted in the following circumstances:

(a) When calculation of the deduction for consumption tax on purchases by the proportional method has resulted in a material change in the percentage of taxable sales and;

(b) When the use of fixed assets subject to adjustment has been changed from exclusive use for non-taxable business to exclusive use for taxable business, or vice versa.

- (2) With respect to the amount of tax on taxable purchases of inventories, adjustment is made in the following circumstances:

(a) When a tax-exempt enterprise has become a taxable enterprise and;

(b) When a taxable enterprise has become a non-taxable enterprise.

3. Simplified Tax System

Taking the administrative burden of small and medium-sized enterprises into account, a simplified tax system has been designed to help them easily calculate deductible tax on purchases based on the amount of consumption tax on sales.

Through a revision in 2003, the upper limit to the application was reduced from taxable sales of ¥200 million to ¥50 million, to be effective from the taxation period beginning on April 1, 2004 onward.

a. Simplified tax system

Enterprises whose taxable sales during the base period are no more than ¥50 million, can choose to regard the amount calculated by multiplying their taxes on purchases by the deemed rate of purchases defined according to their type of business of their taxes on sales (less the amount of taxes on refunded sales) as tax on taxable purchases. Once this simplified tax system is chosen, it cannot be changed for two years.

b. Applicable tax period

This simplified tax system is applicable for the tax period following the period when notification is submitted and in each tax period thereafter with taxable sales amounting to no more than ¥50 million for the corresponding base period.

Although advance notification is required, notification submitted during the tax periods below makes this system applicable from that tax period:

- (1) Tax period during which the enterprise concerned started its business in Japan;
- (2) Tax period during which the enterprise concerned inherited the business of an ancestor who also used this system;
- (3) Tax period during which the enterprise concerned merged with the business of an amalgamated corporation which also used this system and;
- (4) Tax period during which the enterprise concerned divided for absorption with the business of a divided corporation which also used this system.

With respect to the determination of taxable sales of a subsidiary formed through divisions or of the dividing parent corporation for the base period, taxable sales of the parent corporation or of the subsidiary for the base period are taken into accounts. However, taxable sales of a merger corporation or of a divided and succeeding corporation, or of a dividing corporation are determined based on their taxable sales for the base period.

c. Deemed rates of purchases

- Type 1 businesses: 90%

Type 1 businesses corresponding to wholesalers

- Type 2 businesses: 80%

Type 2 businesses corresponding to retailers

- Type 3 businesses: 70%

Type 3 businesses corresponding to those listed below.

- Agriculture
- Construction
- Forestry
- Manufacturing (including manufacturing retailers)
- Fishery
- Electricity, gas, heat, or water supply
- Mining

- Type 4 businesses: 60%

- Type 5 businesses: 50%

Type 5 businesses corresponding to those listed below.

- Real estate
- Transport and communication
- Service industry (except restaurants)

Type 4 businesses corresponding to those other than Type 1, 2, 3, or 5.

The rates should be applied to all sales of an enterprise.

d. Relationship to other deductions

This system provides an exception for calculating the consumption tax deduction on purchases. Therefore, other schemes of deduction (such as the deduction for the consumption tax on the amounts of refunded sales, the deduction for the consumption tax on losses from bad debts) are applicable as separately determined.

During the tax period in which this system is applicable, no adjustment is to be made on the consumption tax deduction amount on purchases of fixed assets subject to adjustment and the deduction for the consumption tax on inventories in conjunction with the shift of status from non-taxable business enterprises to taxable business enterprises.

8/9 Other Deductions

1. Tax Deduction for Refunds of Sale Prices

This deduction is conditional on the maintenance of books or other documents recording the particulars of refunds of sale prices.

In cases where prices of taxable sales are refunded due to the return of goods unsold, discounts, or rebates, the refund of sale prices can be deducted from the amount of consumption tax for the tax period during which such refunds are made.

2. Tax Deduction for Losses from Bad Debts

When, due to circumstances in accounts receivable and other claims on the

buyers, all or part of the compensation for transfers of taxable assets including tax have become unrecoverable, the amount of consumption tax included in the unrecoverable amounts of sales are deductible from the amount of consumption tax during the tax period in which the bad debt takes place.

The application of this deduction is conditional on the maintaining of supporting documents.

8/10 Self Assessment and Payment

1. Domestic Transactions

a. Tax period

(1) General

Tax period is the time frame for which payable amounts of the consumption tax are calculated. Taking into account the taxpayer's burden for tax collection and returns, the tax period is the calendar year for individual proprietors and the accounting period for corporations.

An arrangement has also been made to shorten the tax period, taking into account the interest payment burden from the payment of the consumption tax on purchases by enterprises primarily engaged in export transactions or those who are regular recipients of consumption tax refunds.

(2) Shorter tax periods

When taxpayers so elect, each of the quarters from January to March, April to June, July to September, and October to December, or each of months beginning from January 1 becomes the tax period for individual proprietors, while each of the quarters, or each of months starting from the first month of an accounting period becomes the tax period for corporations.

b. Final return and payment of taxes

Enterprises must file their final return and pay taxes (with the local consumption tax) due within two months of the day following the last day of the tax period. In addition, individual proprietors must file their final return and pay taxes by the end of March of the following year.

c. Interim tax declaration and payment

Businesses (excluding those which selected the period of tax payment as stated in the above a (2)) shall submit their interim tax declaration and pay the tax as indicated in the items stated below unless the annual tax amount paid in the last period for tax payment is no more than ¥480,000.

- ① In the case of a business which paid more than ¥480,000 and ¥4 million or less as the annual tax amount during the last period for tax payment:

An interim declaration shall be submitted within two months from the day

following the end of the period of six months from the day of commencement of the period for tax payment, and the tax in the amount of half as much as the annual tax amount shall be paid as decided by the end of the relevant period.

- ② In the case of a business which paid more than ¥4 million and ¥48 million or less:

An interim declaration shall be submitted within two months from the date following the end of each three-month period from the day of commencement of the last period for tax payment, and the tax shall be paid in the amount of a quarter as much as the annual tax amount as decided by the end of the relevant period.

- ③ In the case of a business which paid more than ¥48 million as the annual tax amount during the last period for tax payment:

An interim declaration shall be submitted within two months from the day following the end of the period of one month from the day of commencement of the period for tax payment (for a month from the day of commencement of the period for tax payment, after passage of two months from the date of commencement of the period for tax payment) and the tax shall be paid in the amount of a twelfth as much as the annual tax amount as decided by the end of the relevant period.

- d. Attachment of certain details to a final return, etc.

Taxpayers are obliged to attach the details of the prices of assets transferred in the tax period, etc., and of the tax amount of taxable purchases, etc., in the tax period to a final return, an interim return, or a return of claim for a refund.

2. Import Transactions

- a. General

- ① Self-assessment system

In the case of goods subject to the self-assessment system under customs law, business enterprises must file tax returns and pay (with the local consumption tax) taxes to the Director of Customs Offices at the time of receipt of taxable goods from bonded areas.

However, when a business enterprise files a special return on tariff with the Custom-House, the enterprise shall pay the taxes to the Custom-House by the end of the following month of the day that the enterprise files a return and takes goods out of the bonded area.

- ② Official assessment system

In the case of goods subject to the official assessment system, business

Consumption Tax

enterprises must file assessment case returns to the Director of Customs Offices and the director must collect the consumption tax (with the local consumption tax).

b. Deferment of payment (in the case of ①)

① Deferment on a one-time basis

Payment can be deferred for a period up to three months each time the goods are delivered if collateral is offered.

② Deferment on a one-month basis

Payment of tax for a specific month can be deferred for a period up to three months from the end of that month if collateral is offered.

③ Deferment of special returns

When a guarantee is submitted to the Custom-House, payment can be deferred up to two months from the end of the month when the enterprise is supposed to take goods out of the bonded area.

8/11 Special Provisions Concerning Government and Entities

1. Special Provisions Concerning National and Local Governments

a. Unit of calculation

The national government and local public bodies are regarded as one corporation for each of their general accounts and special accounts.

b. Time of asset transfers, etc.

Asset transfers, etc. and taxable purchases by the national government or local public bodies can be regarded as being made on the last day of the accounting year during which receipt or payment of compensation is made.

2. Special Provisions Concerning Deductions on Purchases

With respect to the national government, local public bodies, corporations listed in Schedule 3 of the Consumption Tax Law, and associations and foundations without juridical personality, the amount of tax on purchases corresponding to specific revenue (such as taxes, subsidies, and donations) is excluded from deduction.

With respect to the general accounts of the national government and local public bodies, the amount of consumption tax on sales and the aggregate amount of various deductions are regarded as identical and the bodies are therefore exempt from filing tax returns.

3. Special Provisions Concerning Due Date for Tax Returns

With respect to the national government and local public bodies, exceptions are provided concerning the due date for tax returns.

The due dates are the following months after the settlement of the accounting period:

National government	5 months
Local government	6 months
Local public corporation	3 months

8/12 Obligation to Show Gross Price

When a taxable business in order to transfer a taxable asset to a consumer indicates the price of the asset in advance by means of a tag or advertisement, the undertaker shall indicate the total amount paid including the relevant consumption tax and local consumption tax. This provision initially established in the revision of FY 2003 will be applicable from April 1, 2004 onward.

(reference) Local Consumption Tax

a. General

The Local Consumption Tax (Prefectural Tax) was established on April 1 1997 to replace the Consumption Transfer Tax in order to build strong finances or local finances to promote decentralization and to enhance local welfare.

b. Taxpayer

The business and the person to receive foreign cargoes from the bonded area (consumption tax payer)

c. Tax Base

- (1) As for domestic transactions, the tax base is the amount of the Consumption Tax.
- (2) As for import transaction, the tax base is the amount of the Consumption Tax levied on the receipt of taxable cargoes from bonded areas.

d. Tax Rate

The tax rate is 25% of the amount of consumption tax (equivalent to a consumption tax rate of 1%)

e. The assessment and Payment

- (1) The enterprises that are required to file a final return must file a final return with that of Consumption Tax and pay the declared Local Consumption Tax amount with the Consumption Tax amount by the deadline for declaration of Consumption Tax.

Consumption Tax

- (2) Those who receive taxable cargoes from bonded areas must file a fixed return with that of Consumption Tax to the Director-General of Customs and pay the declared Local Consumption Tax amount with the Consumption Tax amount.

[Note 1] The enterprises declare and pay Local Consumption Tax with the same return and receive a tax payment slip including the Consumption Tax.

[Note 2] While Local Consumption Tax is a Prefectural Tax, the State is executing this tax with Consumption Tax for the time being considering the burden of taxpayers, etc.

CHAPTER IX

LIQUOR TAX

9/1 General

1. Method of Taxation on Liquor

Liquor tax is currently imposed on liquor* shipped from manufacturing premises and on imported liquor* withdrawn from bonded areas.

2. Characteristics of Liquor Tax Administration

Liquor tax revenue comprises a relatively large percentage of total tax revenue. Tax rates for liquor are higher than for other commodities. The following measures are taken to collect this tax.

a. License for Manufacturing or Sale of Liquors

Those who intend to manufacture or to sell liquor must obtain a license from the director of the relevant Tax Office is required for each kind of liquor and for each premises for production or sales. This license system was established to secure liquor tax revenue and, at the same time, to guarantee the quality of liquor.

Anyone manufacturing liquor without a license is subject to a fine not exceeding ¥500,000, penal servitude not exceeding five years, or both. Anyone selling liquor without a license is subject to a fine not exceeding ¥200,000, penal servitude not exceeding one year, or both. The following table shows the number of licensed liquor-manufacturing premises as of the end of March 2004, the total quantity of liquor shipped from manufacturing premises and withdrawn from bonded areas, and the amount of tax thereon for various kinds of liquor.

* In the Liquor Tax Law, “liquor” refers to beverages containing 1% or more ethyl alcohol by volume.

Taxable Quantity and Revenue from Liquor Tax

Kind	Number of licensed liquor manufacturing premises	Quantity of Ship-ment and with-drawal in FY 2004	Amount of Liquor Tax in FY 2004
		(Thousands of kl)	(Millions of yen)
<i>Sake</i>	2,087	753	94,963
<i>Sake</i> compound	78	64	4,961
<i>Shōchū</i> Group A	119	519	122,025
<i>Shōchū</i> Group B	840	534	126,277
<i>Mirin</i>	104	108	2,296
Beer	315	3,837	850,097
Wine, etc.	593	248	16,998
Whisky & brandy	191	97	37,071
Spirits	368	81	11,099
Liqueur	604	732	64,325
Others	670	2,579	328,713
Total	5,969	9,552	1,658,825

Notes: (1) Classifications before the tax reform 2006 are described above.

(2) *Shōchū* is an alcoholic distillate of fermented sweet potato mash, etc., containing no more than 45% (with respect to Group A, less than 36%) ethyl alcohol by volume. Group A is distilled continuously; Group B, otherwise.

(3) *Mirin* is sweet *sake* or liqueur made from rice, etc., and is used as seasoning as well as an liquor.

The number of licensed liquor-manufacturing premises at the end of March 2005 is as follows:

Wholesalers	14,417
Retailers	197,411
Others	284
Total	212,112

b. Inspection and Supervision

In collecting liquor tax, the National Tax Agency exercises strict inspection and supervision of liquor manufacturers.

c. Administration of the Law Concerning Liquor Business Associations and Measures for Securing Revenue from the Liquor Tax

The Law concerning Liquor Business Associations and Measures for Securing Revenue from the Liquor Tax has been enacted to secure revenue from

liquor tax and ensure stability in the sales of liquor.

Established according to this law, there are liquor manufacturer associations and liquor seller associations comprising liquor business associations subject to Ministry of Finance control facilities, purchases of raw materials, quantity of sales, selling prices, etc. Per the law, the Minister of Finance can issue various recommendations or orders to liquor business associations, liquor manufacturers, and liquor sellers including non-members.

9/2 Taxpayers

In principle, those who manufacture or withdraw liquor from bonded areas are to pay liquor tax on the liquor shipped from the manufacturing premises or withdrawn from bonded areas. The term “shipment” in this instance means the transfer of liquor from the manufacturing premises in a physical sense. Then, liquor consumed or remaining on the manufacturing premises when the manufacturing license of liquor is invalidated are deemed to have been shipped from the manufacturing premises for the purpose of the Liquor Tax Law. When liquor is shipped from or consumed on the manufacturing premises for reasons for which the manufacturer is not responsible, liquor tax due is collected from the consumer or shipper concerned rather than the manufacturer.

9/3 Tax Base and Tax Rates

The liquor tax is based on the quantity of liquor (unit tax).

In the 1989 tax reform, an ad valorem liquor tax and a grading system for Japanese sake and whiskey were abolished.

The tax rates are shown in the table below.

Liquor Tax Rates (Example)

Kind		Tax rate (per kl)	Additional amount of tax per 1% of al- cohol
Sparkling Alcohol Drinks (beer etc.)		¥220,000	—
	Low malt beer (the ratio of malt not less than 25% and less than 50%)	¥178,125	—
	Low malt beer (the ratio of malt less than 25%)	¥134,250	—
	Others (except hop-based liquors)	¥80,000	—
Fermented Liquor		¥140,000	—
	Refined <i>Sake</i>	¥120,000	—
	Wine	¥80,000	—

Liquor Tax

<i>Shochu</i> etc.	(20% of alcohol) ¥200,000	¥10,000
Whisky, Brandy, Spirits	(37% of alcohol) ¥370,000	¥10,000
Miscellaneous liquor	(20% of alcohol) ¥220,000	¥11,000
<i>Sake</i> compound	¥100,000	—
<i>Mirin</i>	¥20,000	—
Sweet wine or Liqueur	(12% of alcohol) ¥120,000	¥10,000
Powdered Liquor	¥390,000	—

9/4 Tax Exemption

Under the Liquor Tax Law, the following tax exemptions are granted:

a. Suspension of Tax

Liquor tax is exempt when liquor are transferred from one manufacturing site to another (tax suspended transfer), or when they are delivered from bonded areas (tax suspended dealing) as raw material for other kinds of liquors.

b. Tax Exemption for Exports

Liquor shipped from one manufacturing site to another for export are tax exempt, provided that manufacturers submit a detailed statement about the exported liquor. The export exemption is based on the principle that the liquor tax be imposed on the consumption of liquor in Japan.

9/5 Assessment and Payment

1. Liquor manufacturers must submit a return to the Director of the relevant Tax Office reporting liquor by classification and quantity and the amount of the liquor tax by the end of the next month following shipment; they must pay the tax by the end of the next month following the tax return was submitted.
2. Those withdrawing liquor from a bonded area must submit a return to the Directors of Custom-House and pay the tax before doing so. However, when they are going to file a special return on tariff with the Custom-house, they shall file such a special return on tariff and pay the tax by the end of the following month of the current month when they take goods out of the bonded area.
3. Liquor tax payment may be postponed for up to one month by those who manufacture or withdraw liquor on condition that something is provided as if special difficulties in payment arise.

CHAPTER X

TOBACCO TAX

10/1 General

With the transformation of the tobacco industry from a monopolized public corporation into an ordinary stock company, a special charge on corporation profit was replaced by a tobacco excise tax in April 1985. This indirect tax is imposed on cigarettes, tobacco for pipes, cigars and other tobacco products shipped from production premises or withdrawn from bonded areas. With the introduction of the consumption tax in April 1989, the tobacco excise tax was renamed the tobacco tax and unified the taxation method from a system combining an ad valorem tax and unit tax to a unit tax system.

10/2 Taxpayers

The tobacco tax is levied on manufacturers of tobacco products or those who have withdrawn them from bonded areas.

10/3 Tax Base

Specific duties are imposed on tobacco. The tax is based on the number of cigarettes. Two grams of cut tobacco or cigars and two grams of cut tobacco, chewing tobacco, or snuff are as treated equivalent to one cigarette.

10/4 Tax Rates

Tax rates are shown in the table below. It should be noted that a local tobacco tax and a special tobacco tax are levied in addition to the national tobacco tax.

Tobacco Tax Rates

Class	
Cigarettes	¥3,552/per thousand
Pipe tobacco	〃
Cigars	〃
Cut tobacco, chewing tobacco and snuff	〃

10/5 Tax Payment

Manufacturers of tobacco products must file a return with the Director of the Tax Office describing the tax base quantity of tobacco and the tax amount for each class. They must file the return and pay the tax by the end of the next month following the shipment of the products from production premises. A person who takes tobacco products out of the bonded area shall also file a return with the Custom-House and pay the tax before the person takes the products out of the bonded area. However, when a person is going to file a special return with the Custom-House, the person shall file such a return with the Director of the Custom-House and pay the tax by the end of the following month of the month when the person takes the products out of the bonded area.

If the taxpayer furnishes security for his or her tax liability, the tobacco tax payment may be postponed for up to a month for manufacturers and two months for importers. (One month for an importer who files a special return with the Custom-House)

10/6 Others

Exports are exempted from tobacco tax. Tax on shipment to another production premise is suspended and tax credits or refunds are provided for products returned to production premises.

CHAPTER XI

SPECIAL TOBACCO TAX

11/1 General

The “Special Tobacco Tax” was established and enforced from 1 December 1998 in consideration of the increased burden on general accounts after assuming debts related to long-term loans, etc., for the Japan National Railway Settlement Corporation and debts related to loans, etc. of the National Forestry Business Special Account.

The special tobacco tax is currently a temporary measure.

11/2 Taxpayers

The same as for the tobacco tax (see 10/2).

11/3 Tax Base

The same as for the tobacco tax (see 10/3).

11/4 Tax Rates

Class	
Cigarettes	¥820/per thousand
Pipe tobacco	〃
Cigars	〃
Cut tobacco, chewing tobacco, and snuff	

11/5 Tax Payment

The special tobacco tax is declared and paid when the tobacco tax is declared (see 10/5).

11/6 Others

Tobacco exempt from the tobacco tax by provisions of the Tobacco Tax Law concerning suspension of tax on shipment or exemption of tax or exports are exempt from the special tobacco tax (see 10/6).

CHAPTER XII

GASOLINE TAX

12/1 General

The gasoline tax is imposed on gasoline* shipped from refineries or withdrawn from bonded areas.

Revenue from the gasoline tax is first credited to the General Accounts of the State and then transferred to the Road Construction and Improvement Special Account**, according to The Special Law relating to Revenues from Charges for Road Maintenance. The revenue from this tax is earmarked for road construction and improvement under that law.

The gasoline tax is collected together with the local road tax (see 16/1).

12/2 Taxpayers

Those who ship gasoline from refineries or withdraw gasoline from bonded areas must pay the gasoline tax.

12/3 Tax Base

Gasoline tax is based on the quantity of gasoline shipped from refineries or withdrawn from bonded areas after deducting expected losses in storage and transit. If gasoline is consumed at a refinery or a bonded area, it is regarded as having been shipped or delivered from those areas.

12/4 Tax Rate

¥48,600*** per kilolitre of gasoline.

12/5 Tax Payment

Those who ship gasoline are required to file a return with the Director of the Tax Office describing the quantity of gasoline shipped and the amount of the gasoline

* “Gasoline” is defined as hydrocarbon oil with a specific gravity not exceeding 0.8017 at 15°C.

** One-fourth of the revenue from the tax will be put directly into the Road Maintenance Special Account for local road maintenance from 1 April 2003 to 31 March 2008.

*** This tax rate is applicable to gasoline that is shipped from refineries or is withdrawn from bonded areas from 1 December 1993 to 31 March 2008.

tax and shall pay the tax by the end of the month following the shipment. If gasoline is withdrawn from a bonded area, a return should be filed with the Director of the Custom-House. However, when they are going to file a special return on tariff with the Custom-House, they shall file such a special return on tariff and pay the tax by the end of the following month of the current month when they take goods out of the bonded area.

If the taxpayer furnishes security for the tax liability, payment of the gasoline tax may be postponed for up to two months for shipments from refineries, three months for withdrawals from bonded areas and two months for exceptional declaration of customs.

Like other indirect tax laws, the Gasoline Tax Law exempts exports from tax, suspends the tax for shipment from refineries to other refineries as raw material for new gasoline, and provides credits or refunds of the tax on gasoline reshipped from refineries.

Furthermore, the Special Taxation Measures Law stipulates that no tax is imposed on gasoline consumed as raw material for petrochemicals for the time being, or on gasoline consumed as fuel for electric power or as solvent for rubber until March 31, 2008.

CHAPTER XIII

LIQUEFIED PETROLEUM GAS TAX

13/1 General

Liquefied petroleum gas tax is an indirect tax imposed on liquefied petroleum gas put into fuel tanks of automobiles. Methane and ethane are not subject to the tax.

13/2 Taxpayers

Persons who put liquefied petroleum gas into fuel tanks of automobiles or those who receive taxable petroleum gas from a bonded area are required to pay the tax.

13/3 Tax Base

The tax is based on the quantity of the taxable gas shipped from a filling station or withdrawn from bonded areas. When the taxable gas is measured by volume, one liter of the taxable gas is regarded as 0.56 kg (the conversion through the specific gravity of that gas may be used if permitted by the Director of the Tax Office).

13/4 Tax Rate

¥17.5 per kilogram.

13/5 Tax Payment

Taxpayers must file a return with the Director of the Tax Office by the end of the month following the shipment and pay the tax within one month thereafter. If the taxable gas is to be withdrawn from bonded areas, those who plan to withdraw such gas should file a return and pay tax to the director of the custom house before its withdrawal.

However, when they are going to file a special return on tariff with the Custom-House, they shall file such a special return on tariff and pay the tax by the end of the following month of the current month when they take goods out of the bonded area.

If a taxpayer provides collateral for the tax obligation, and the taxpayer ships gas from a filling station or withdraws gas from a bonded area, then the due date can be postponed up to one month (excluding the case when the taxpayer files a special

return on tariff.).

13/6 Others

Like other indirect tax laws, the Liquefied Petroleum Gas Tax Law exempts exports from taxation. And it allows to postpone payment, and provide for credits or refunds of the tax on gas reshipped to a filling station.

CHAPTER XIV

AVIATION FUEL TAX

14/1 General

The aviation fuel tax is an indirect tax imposed on aviation fuel loaded on aircraft, including helicopters, in the territory of Japan, except for international flights.

Eleven-thirteenths of the revenue from the tax is credited to the General Accounts of the State and then transferred to the Airport Construction and Improvement Special Account.

The remaining 2/13 of the revenue is granted to local governments to be earmarked for expenditures related to airports.

14/2 Taxpayers

Taxpayers of the aviation fuel tax are as follows:

- (a) Owners of aircraft
- (b) Where it is clearly shown by the contract that persons other than owners are “users of aircraft” as prescribed by the Aviation Act, these users of aircraft instead of owners
- (c) Where owners or users of aircraft have no residence or office in Japan, pilots-in-command instead of owners or users of aircraft
- (d) Persons other than owners, users, and pilots-in-command who make test flights or repairs of aircraft
- (e) Persons who make repairs of or conduct test runs of aircraft engines themselves (in this case, the tax is imposed on the quantity of aviation fuel consumed for repairs or test runs)

National and local governments are exempted from the aviation fuel tax.

14/3 Tax Base

Aviation fuel tax is based on the quantity of aviation fuel loaded on aircraft.

14/4 Tax Rate

¥26,000 per kiloliter.

14/5 Tax Payment

Taxpayers are required to file a return and pay the tax by the end of the month following the loading of fuel on their aircraft.

CHAPTER XV

PETROLEUM AND COAL TAX

15/1 General

Petroleum and Coal tax is imposed on crude petroleum shipped from extracting stations (domestic production) or on crude petroleum or specified petroleum products withdrawn from bonded areas (imports) from 1 June 1978.

Imported petroleum products are taxed to avoid discrimination against products manufactured from crude petroleum that have been subjected to the tax.

Petroleum and Coal tax is imposed on gaseous hydrocarbons shipped from extracting stations (domestic production) or withdrawn from bonded areas (imports) as of 1 September 1984.

From October 1, 2003, petroleum and coal tax shall be imposed on domestic coal moved from the extracting area or on imported coal withdrawn from a bonded area.*

The revenue from the petroleum tax is first credited to the General Accounts of the State and then transferred to the Special account for measures to improve energy supply and demand structure, as appropriated in the yearly budget. The funds of the Special account for measures to improve energy supply and demand structure are used for various programs to secure a stable supply of petroleum and to develop and introduce alternative energy sources.

15/2 Taxpayers

Those who ship crude petroleum, gaseous hydrocarbons or coal from extracting stations or withdraw crude petroleum, petroleum products, gaseous hydrocarbons or coal from bonded areas must pay the petroleum tax.

15/3 Tax Base

(1) Taxable petroleum, etc., defined

Taxable crude petroleum is “petroleum oils and oils obtained from bituminous minerals or crude,” as defined in No. 2709.00 of the annexed table of the Customs Tariff Law.

Petroleum products, taxable when withdrawn from bonded areas, are “petroleum oils and oils obtained from bituminous minerals, other than crude, or

*Following the imposition of tax on coal, the name “petroleum tax” was revised to “petroleum and coal tax.”

preparations of petroleum oils, or oils obtained from bituminous minerals,” as defined in No. 2710,11 and No. 2710,19 of the same table, i.e., gasoline, kerosene, gas oils, heavy fuel oils and raw oils, lubricating oils, and other such liquids.

Gaseous hydrocarbons are taxable when they are shipped from extracting stations or withdrawn from bonded areas. They are “petroleum gases and other gaseous hydrocarbons,” as defined in No. 27.11 of the aforementioned table.

The coal is taxable when it is moved from the extracting area or withdrawn from a bonded area. It is “coal, briquettes, oval briquettes and other solid fuels similar to them” as referred to in Item 27.01 in the table the products of coal.

(2) Tax base

The tax base was changed from price to quantity as of 1 August 1988.

The tax is based on the quantity of crude petroleum, gaseous hydrocarbons or coal shipped from extracting stations or of crude petroleum, petroleum products, gaseous hydrocarbons or coal withdrawn from bonded areas.

15/4 Tax Rates

Tax rates are as follows:

	April 1, 2005	April 1, 2007
Crude petroleum or imported petroleum products; (per kl;)	¥2,040	¥2,040
Natural gas (per tonne)	¥960	¥1,080
Gaseous hydrocarbons (except natural gas) (per tonne)	¥940	¥1,080
Coal (per tonne)	¥460	¥700

15/5 Tax Payment

Those who ship crude petroleum, gaseous hydrocarbons or coal from extracting stations are required to file a return with the Director of the Tax Office and shall pay the tax by the end of the month following shipment.

Those who withdraw crude petroleum, petroleum products, gaseous hydrocarbons or coal from bonded areas shall file a return with the Director of the Customs House and shall pay the tax by the time of withdrawal. However, when they are going to file a special return on tariff with the Custom-House, they shall file such a special return on tariff and pay the tax by the end of the following month of the current month when they take goods out of the bonded area. However, a regular

Petroleum And Coal Tax

importer may file a return and pay the tax by the end of the month following the withdrawal if he or she receives the approval of the Commissioner of the National Tax Agency.

If the taxpayer furnishes security for his or her tax liability, the payment of the petroleum tax may be postponed for up to two months for shipment from extracting stations and three months for withdrawal from bonded areas (two months when the taxpayer declares exceptionally and receives the approval of the Commissioner of the National Tax Agency).

15/6 Others

The Petroleum and Coal Tax Law, like other indirect tax laws, exempts exports from tax, suspends the tax for shipment from an extracting station to the place approved by the director of the tax office, and provides credits or refunds of the tax on crude petroleum, gaseous hydrocarbons or coal reshipped from the station.

No tax is imposed on gaseous hydrocarbons shipped by extractors (excluding corporations) of gaseous hydrocarbons for the exclusive purpose of consumption by themselves or their relatives living with them.

It is further stipulated temporarily in the Special Taxation Measures Law that, prior to March 31, 2008, the petroleum and coal tax is not levied on imported naphtha, kerosene, or light fuel oil to be used for petrochemicals production, imported LPG to be used for ammonia production, or imported heavy fuel oil A to be used in agriculture, forestry, or fishery; the tax will be refunded if those who ship these materials from refineries produce naphtha, kerosene, or light fuel oil to be used for petrochemicals production or heavy fuel oil A to be used in agriculture, forestry, or fishery.

Till March 31, 2007 petroleum and coal tax shall not be imposed on imported coal for production of iron and steel, coke and cement.

Also, till March 31, 2007 petroleum and coal tax shall not be imposed on imported coal for power generation in Okinawa prefecture.

In the case that the oil, asphalt, etc. made from taxed crude oils, etc. are taken out of the plant or spent in the plant as fuel, the amount corresponding to the Petroleum Tax amount is refunded until 31 March 2007, assuming that the oil, asphalt, etc. were subject to this tax.

CHAPTER XVI

LOCAL ROAD TAX

16/1 General

The local road tax, like the gasoline tax, is an indirect tax imposed on gasoline that is shipped from refineries or withdrawn from bonded areas (see 12/1).

The method of taxation, with the exception of tax rates, is similar to that of the gasoline tax, and the tax is paid together with the gasoline tax. The revenue from the local road tax is granted to local governments according to prescribed formulas. The revenue from the tax is earmarked for construction and improvement of local roads.

16/2 Taxpayers

The same as in the case of the gasoline tax (see 12/2).

16/3 Tax Base

The same as in the case of the gasoline tax (see 12/3).

16/4 Tax Rate

¥5,200 per kilolitre of gasoline *.

16/5 Tax Payment

The same as in the case of the gasoline tax (see 12/5).

* This tax rate is applicable to gasoline that is shipped from refineries or is withdrawn from bonded areas as of 1 December 1993 to 31 March 2008.

CHAPTER XVII

MOTOR VEHICLE TONNAGE TAX

17/1 General

Motor vehicle tonnage tax is imposed on motor vehicles for which a motor vehicle inspection certificate or, in the case of inspection-exempt light motor vehicles*, a registration number is obtained. Details for the inspection certificate and registration are provided in the Vehicles for Road Transportation Law.

Two-thirds of the revenue from the tax is credited to the General Accounts of the State. The remaining one-third, which is granted to local governments, is earmarked for construction and improvement of local roads.

17/2 Taxpayers

Users of motor vehicles who obtain a motor vehicle inspection certificate or, in the case of light motor vehicles, a registration number, are required to pay the motor vehicle tonnage tax at the time of inspection or registration.

17/3 Tax Rates**

Class 1

Motor vehicles with a three-year inspection certificate

① Private passenger vehicles, excluding light motor vehicles

vehicle weight of no more than half a tonne ¥18,900

vehicle weight in excess of half a tonne ¥18,900 for each half-tonne or fraction thereof

* Light motor vehicles are defined as follows:

	Cylinder capacity	Length	Width	Height
Two-wheeled	no more than 250cc over 125cc	no more than 2.5metres	no more than 1.3metres	no more than 2.0metres
Others	no more than 660cc	no more than 3.4metres	no more than 1.48metres	

They are divided into those that require a motor vehicle inspection certificate and those that do not.

A user of a light motor vehicle that requires no motor vehicle certificate is required to report to the Director of the Land Transportation Bureau and must obtain a designated vehicle number.

Light motor vehicles that need no motor vehicle inspection certificate include two wheeled light motor vehicles, caterpillar light motor vehicles, light motor sledges, etc.

** These tax rates are applicable to motor vehicles for which a motor vehicle inspection certificate or a registration number has been obtained from 1 May 1976 to 30 April 2008.

② Light motor vehicles (private passenger vehicles)
¥13,200

③ Motorcycles*

- (i) private use ¥5,100
- (ii) business use ¥7,500

Class 2

Motor vehicles with a two-year inspection certificate

① Private passenger vehicles, excluding motorcycles and light motor vehicles
vehicle weight of no more than half a tonne ¥12,600

vehicle weight in excess of half a tonne ¥12,600 for each half-tonne or fraction thereof

② Vehicles other than private passenger vehicles, motorcycles, and light motor vehicles (mainly vehicles for cranes)

(i) private use

gross vehicles weight of no more than 1 tonne ¥12,600

gross vehicles weight in excess of 1 tonne ¥12,600 for each tonne or fraction thereof

(ii) business use

gross vehicles weight of no more than 1 tonne ¥5,600

gross vehicles weight in excess of 1 tonne ¥5,600 for each tonne or fraction thereof

③ trucks weighing no more than 2.5 tonne

(i) private use

gross vehicles weight of no more than 1 tonne ¥8,800

gross vehicles weight in excess of 1 tonne ¥8,800 for each tonne or fraction thereof

(ii) business use

gross vehicles weight of no more than 1 tonne ¥5,600

gross vehicles weight in excess of 1 tonne ¥5,600 for each tonne or fraction thereof

④ Motorcycles

(i) private use ¥5,000

* A category of “Motorcycles with a three-year effective certificate” is made by a cabinet order within a year from the promulgation of the “Law to Partially Amend the Road Transport Law (May 19, 2006, the 40th law)”.

Motor Vehicle Tonnage Tax

- (ii) business use ¥3,400
- ⑤ Light motor vehicles
 - (i) private use ¥8,800
 - (ii) business use ¥5,600

Class 3

Motor vehicles with a one-year inspection certificate

- ① Taxis and hired cars
 - vehicle weight of no more than half a tonne ¥2,800
 - vehicle weight in excess of half a tonne ¥2,800 for each half tonne or fraction thereof
- ② Trucks and buses
 - (i) private use
 - gross vehicle weight of no more than 1 tonne ¥6,300
 - gross vehicle weight in excess of 1 tonne ¥6,300 for each tonne or fraction thereof
 - truck with gross vehicle weight of no more than 2.5 tonnes
 - gross vehicle weight of no more than 1 tonne ¥4,400
 - gross vehicle weight in excess of 1 tonne ¥4,400 for each tonne or fraction thereof
 - (ii) business use
 - gross vehicle weight of no more than 1 tonne ¥2,800
 - gross vehicle weight in excess of 1 tonne ¥2,800 for each tonne or fraction thereof
- ③ Motorcycle
 - (i) private use ¥2,500
 - (ii) business use ¥1,700
- ④ Light motor vehicle that needs a vehicle inspection certificate
 - (i) private use ¥4,400
 - (ii) business use ¥2,800

Class 4

Light motor vehicle that needs no vehicle inspection certificate (only for light vehicle assigned vehicle number)

- ① Two-wheeled
 - (i) private use ¥6,300
 - (ii) business use ¥4,500
- ② Others

(i) private use	¥13,200
(ii) business use	¥8,400

17/4 Tax Payment

A motor vehicle user, including that of a light motor vehicle, is required to submit a payment statement of motor vehicle tonnage tax to the Director of the relevant Land Transportation Bureau* affixing stamps when he or she obtains a motor vehicle inspection certificate or a designated vehicle number.

Under special circumstances, he or she may pay the tax in cash instead of stamps. In this case, he or she may pay in cash at certain banks or post offices and submit the receipt issued by the bank or post office to the Director of the regional Land Transportation Bureau.

17/5 Tax Exemption

Large, dedicated-use motor vehicles such as bulldozers and used light motor vehicles that need no vehicle inspection certificate are exempt from the tax.

17/6 Other

In the case where the director of the Transport Bureau, etc., confirmed that a used motor vehicle handed over to a pick-up trader on and after January 1, 2005, was properly scrapped, the amount of motor vehicle tonnage tax equivalent to the remaining period of the valid period of the motor vehicle inspection certificate will be refunded.

* For a light motor vehicle needing a motor vehicle inspection certificate, the user should pay the tax to the Light Motor Vehicle Inspection Association.

CHAPTER XVIII

PROMOTION OF POWER-RESOURCES DEVELOPMENT TAX

18/1 General

The “Promotion of Power-resources Development Tax” imposed on ordinary electric utility enterprises is earmarked to meet expenses for measures to (1) the promotion of establishing atomic power plants, hydroelectric power plants and geothermal power stations and the smooth operations of such facilities (2) the promotion of using these facilities for power generation and for ensuring safety at these facilities and; (3) the smooth power supply by these power generation facilities.

18/2 Taxpayers

Electric utility enterprises that supply electric power to meet the general public’s demand have to pay this tax.

18/3 Tax Base

The tax is based on the volume of electricity for sale.

Electricity for sale is as follows:

- (1) Electricity that ordinary electric utility enterprises supply to others in compliance with a demand from them, except for electricity that is transferred to other ordinary electric utility enterprises.
- (2) Electricity that ordinary electric utility enterprises themselves consume except for the generation of electric power.

18/4 Tax Rate

	April 1, 2005	April 1, 2007
Electric power sold (per 1000kw/h)	¥400	¥375

18/5 Tax Payment

Every month, taxpayers are required to file a return describing the amount of electricity sold for which payment is due that month, the amount they consumed,

and the amount of tax thereon; they must pay the tax by the end of the following month.

Tax payments should be made to and returns filed with the Director of the Tax Office for the area where the head office of the taxpayer is located.

CHAPTER XIX

PAYMENT OF NATIONAL TAXES

19/1 General

1. The present national tax collection system consists of four separate systems: i) a self-assessment system; ii) an official assessment system; iii) a withholding tax system and; iv) a stamp payment system.
2. i) Under the self-assessment system, taxpayers themselves assume the primary responsibility for calculating the tax base and the amount of tax, filing a return to establish tax liability based on their calculation and paying the tax due at the same time. District Director of the Tax Office, however, reserves the right to correct taxpayers' returns with a correction notice. If a taxpayer does not file a return with the Tax Office, tax authorities determine the tax base and the amount of tax and then issue a determination notice to the taxpayer. Taxpayers are required to pay the tax within one month after such notices are issued. The self-assessment system is applied to most direct taxes, such as income tax, corporation tax, inheritance tax, gift tax, and most indirect taxes such as the consumption tax, liquor tax, tobacco tax, gasoline tax, and the liquefied petroleum gas tax. The estimated payment system is used for individual income tax. Under this system, the amount of estimated tax to be prepaid is determined on the basis of the final return from the preceding year, and a taxpayer receives a refund if he or she has paid the estimated tax more than the amount of the tax liability or if he or she pays tax if the amount of the estimated tax is less than the tax liability at the time of the final return (see 2/6, 3 and 4).
- ii) The official assessment system is applicable only to indirect taxes relating to (1) imports that are brought in by persons upon entering Japan and (2) items for which conditions for tax exemption are not satisfied. Under this system, the government determines the tax base and the amount of tax and issues a notice requiring taxpayers to pay the tax. Taxpayers are usually required to file returns, regarded as informative returns, which are different from those under the self-assessment system. Taxpayers must pay the tax by the due date stipulated in the notice of payment.
- iii) The withholding tax system is used for such income items as interest, dividends, wages, and salaries. Those who pay such items of income are required to withhold the proper amount of tax when payment of such an item is made, and in turn, pay the tax on behalf of the recipients no later than the

10th of the following month. If those who pay these items of income —194— fail to withhold or to pay the tax withheld, the tax authorities issue a notice of payment requesting them to pay. This process is similar to that of the official assessment system.

- iv) The stamp payment system is applied to the stamp tax, motor vehicle tonnage tax, and registration and license tax. In those cases, a taxpayer pays tax by affixing a stamp to a document or an account book. However, cash payment instead of a stamp payment is required in some cases.

The table below shows the national taxes and their corresponding systems of collection.

National Taxes and Their Respective Collection System

National Taxes	Collection Systems
Income tax	Self-Assessment and Withholding
Corporation tax	Self-Assessment
Inheritance tax and Gift tax	Self-Assessment
Aviation fuel tax	Self-Assessment
Registration and license tax	Stamp Payment*
Motor vehicle tonnage tax	Stamp Payment*
Land Value tax	Self-Assessment
Consumption tax	Self-Assessment**
Liquor tax	Self-Assessment**
Tobacco tax	Self-Assessment**
Liquid petroleum gas tax	Self-Assessment**
Gasoline tax	Self-Assessment**
Petroleum and Coal tax	Self-Assessment**
Local road tax	Self-Assessment**
Stamp tax	Stamp Payment***
Promotion of power-resources development tax	Self-Assessment

19/2 Agencies Collecting National Taxes

National taxes are paid to the Bank of Japan, the agents thereof, and tax officials. The agents of the Bank of Japan consist of the head and branch offices of com—

* Cash payment is required in some cases.

** In the case of imports brought in by individuals upon entering Japan, and when conditions for tax exemption are not satisfied, official assessment is applicable.

*** Self-assessment is applicable in exceptional cases.

Payment of National Taxes

mercial banks and post offices.

Tax officials collect tax payments when they visit the taxpayer's office or home or when the taxpayer brings a tax payment to the Tax Office.

All revenue is ultimately received by the Bank of Japan and constitutes a deposit with the government.

19/3 Budgetary Procedures for Receipt of National Taxes

National tax collections go into the Adjustment Fund of National Tax Receipts upon receipt and overpaid tax is refunded from this fund, thereby eliminating the restriction to refunds imposed by the limited availability of appropriated funds in the budget. The remainder of the fund is finally taken in as revenue. National taxes, accordingly, are not treated as revenue directly, but are first entered in this Adjustment Fund.

CHAPTER XX

PENALTIES ON NATIONAL TAXES

20/1 General

Penalties are provided in both administrative and judicial forms if taxpayers fail to meet their tax obligations by, for example, neglecting to file tax returns in accordance with tax laws or making incorrect tax returns by omitting taxable income.

An administrative penalty is one of the sanctions taken against a default such as failure to file a tax return or filing a false return. In such cases, “delinquent tax” or “additional tax” is levied on the defaulting taxpayer according to tax law.

Another sanction is a judicial penalty imposed against tax crimes in connection with the assessment and collection of tax. The grounds for such penalties, as well as their nature and extent (a term of penal servitude and amount of fine), are stipulated in tax laws. In view of the specialized nature of tax crimes, the National Tax Violation Control Law provides for investigation, procedures, etc., concerning tax crimes.

20/2 Supplementary Taxes

1. Delinquent Tax

If a taxpayer fails to pay tax by the due date, he or she is obliged to pay, in addition to the principal tax, a delinquent tax fee at the rate of 14.6% per annum from the day following the statutory due date until the actual payment date. However, the rate of delinquent tax is reduced to 7.3% per annum for two months from the day following the statutory due date.

As for the 7.3% delinquent tax rate, there is an exceptional measure such that the rate can be reduced to the official discount rate plus 4%.

2. Additional Tax

The following additional taxes are imposed as administrative penalties:

- a.** Additional tax for deficient returns shall be collected at the rate of 10% of the increased amount of tax incurred by correction or an amended return.
- b.** If the increase in the amount of tax incurred by correction or amendment return exceeds the return filed before the due date or 500,000 yen, additional tax for underpayment shall be collected at the rate of 15% of the excessive amount.

Penalties on National Taxes

- c.** Additional tax for no return or a return filed after the due date shall be collected at the rate of 15% of the amount of tax shown in the return filed after the due date, or tax determined by the government (at the rate of 20% for the amount in excess of 500,000 yen).
- d.** The additional tax on withholding tax determined by government notice of payment or paid after the statutory due date shall be collected at the rate of 10%.
- e.** In the case of fraud, substantial additional tax shall be imposed at the rate of
 - (1) 35% of the tax amount as a penalty for evasion under **a.** and **d.** above and;
 - (2) 40% of the tax amount as a penalty for evasion under **c.** above.

20/3 National Tax Violation Control Law

1. Unless otherwise provided, tax evasion that constitutes a crime is investigated by police or prosecutors and is examined and tried in court, according to the Criminal Procedures Law. Because of their peculiar nature, certain tax crimes require special proceedings. Special experience and knowledge of taxation is required for the investigation of tax crimes and the considerable amount of time and expense needed in settling cases if ordinary proceedings are used (e. g., illegal production of liquor). Accordingly, special procedures for the investigation and punishment of fiscal crimes are stipulated in the National Tax Violation Control Law.
2. Tax officials are authorized to search the premises of suspected tax evaders with a warrant issued by the court.
3. Under the Law, a considerable difference exists between the handling of the evasion of direct taxes and that of indirect taxes. If evasion of direct taxes is involved, the tax official is required, immediately after the investigation, to hand the case over to a prosecutor. The prosecutor then files suit in accordance with ordinary proceedings of the Criminal Procedures Law.
4. If evasion of indirect taxes is involved, the Director of the Tax Office is required to issue a notification to the person suspected of tax evasion, prescribing the amount of the fine, the reasons for the charges and an order to pay the fine at the Tax Office. If the person pays the fine, he or she will not be prosecuted. If they do not pay the fine, immediate prosecution will be undertaken after the case is handed over to a prosecutor.

CHAPTER XXI

COLLECTION OF NATIONAL TAXES

21/1 General

National taxes are collected in accordance with the National Tax Collection Law. The principles of the National Tax Collection Law may also be applied to the compulsory collection of local taxes and other public charges.

In April 1962, the General National Tax Law was promulgated (see 1/1, 2. (3) A.c. and 1/3, 1) and a part of the articles of the National Tax Collection Law was transferred to the General Law, which provides the general procedures for assessment and collection of national taxes.

21/2 Procedure for Collection of National Taxes

Tax authorities must collect national taxes in accordance with the National Tax Collection Law when a taxpayer fails to pay the tax stated on the return at the time of filing, in the notice of correction or determination, or in the notice of payment by the due date.

1. Demand*

When a taxpayer fails to pay tax in full by the due date, the Director of the Tax Office should send a notice of demand within 50 days of that due date.

2. Attachment

If a taxpayer has not paid the tax due within 10 days of the dispatch of the notice of demand, tax collector should attach the taxpayer's properties.

For the purpose of attachment, properties are classified into four categories and different procedures for each category are provided; (1) movable properties and securities; (2) immovable properties, including ships and registered cars, aircraft, etc; (3) claims and; (4) other property rights, including patents and copyrights. In the case of movable properties or securities, for example, the tax collector possesses those properties and attachment takes effect with possession of the properties.

* Stipulated in the General National Tax Law.

3. Request for Share Distribution

If the properties of a delinquent taxpayer are sold at public auction or tender by virtue of execution of other delinquent taxes or of private claims or of other judicial procedures, or bankruptcy procedures are taken, the tax authorities may claim a share of the proceeds distributed from the sale.

4. Sale of Properties

In principle, attached properties are sold publicly by way of tender or auction. The tax authorities make public a notice of the properties to be sold at least 10 days before the date of sale, and also notify the delinquent taxpayer and other parties interested in the intended public sale. The payment must be made by the date when the sale is decided. The buyer acquires ownership of the properties upon payment.

5. Distribution of Proceeds, etc.

The proceeds of the properties sold are appropriated (after costs of disposal) for (1) national taxes for which the properties were attached, (2) national and local taxes and public charges for which a share of the distribution was requested, and (3) credits on properties such as mortgage. Any remainder is delivered to the delinquent taxpayer.

6. Investigation of a Delinquent Taxpayer's Properties

To collect delinquent national taxes, the tax collector may make inquiries of a delinquent taxpayer or those who hold his properties, and may examine books and records concerning those properties. He or she may, if necessary, search the household of the delinquent taxpayer without a warrant. This also applies to third parties who hold properties of the delinquent taxpayer when they refuse to hand over the properties to the collector.

21/3 Other Measures to Secure Collection of National Taxes

In order to collect national taxes in arrear as effectively and promptly as possible, national tax claims are not executed by judicial authorities, but by the tax authorities themselves as prescribed in 21/2. In addition, the following measures are adopted for the same purpose:

1. Priority of National Tax Claims

National tax claims have priority over other public and private claims on a taxpayer's properties except when the private creditors have the right of pledge or hypothecation created prior to the statutory due date of payment, etc. upon the taxpayer's property or when the private creditors have the right of retention or preferential right with respect to tax claims.

2. Extension of Liability for Tax Payment

a. Succession of Liability for Tax Payment*

An heir is responsible for national tax due by a descendant, but those who have accepted succession on the condition that they be liable for the descendant's debts within the limit of his or her assets are liable only to the extent of the value of property received by succession. And those who renounce their claim on inheritance are not liable.

An acquiring corporation or newly created corporation in a merger shall succeed the national tax due by the corporation that ceases to exist due to such a merger.

b. Joint and Several Tax Obligations*

Those who jointly own property or carry out business must assume joint and several obligations for tax liability related to the property or business.

c. Joint Tax liability

When a corporation is divided (not including spin-off divisions), the divided and succeeding corporation, jointly with the other divided corporations, is liable for paying the national taxes that were established before the division. However, the tax liability is limited to the value of the assets to which the succeeding corporation succeeded.

d. Secondary Tax Liability

Sometimes properties that are actually under the control of a certain taxpayer are formally owned by another party. In such cases, an auxiliary tax obligation called "secondary tax liability" equivalent to the taxpayer's liability is imposed on those who formally own such property. This is done to the extent that such an extension of liability is considered justifiable in terms of equity and is tolerable within ordinary civil law.

Among those who have secondary tax liability are; (1) a corporation with its

* Provided in the General National Tax Law.

shares owned by a family, if its stockholder (the delinquent taxpayer) does not have sufficient property other than stocks to pay taxes; (2) those who were taxed on gains from property or business on behalf of persons to whom the gains are nominally attributed (under the principle of attribution of income to an actual beneficiary) and; (3) a transferee of a taxpayer's property without compensation (the case equivalent to "transferee liability" in the U.S. Internal Revenue Code), and so on.

3. Advance Collection*

Under certain circumstances, where a delay will make it impossible for the tax authorities to collect tax (for instance, in the case of liquidation of a corporate taxpayer), the tax authorities may collect the tax immediately regardless of the original due date.

4. Provisional Attachment

When a tax inspection (i.e., fraud case) has been undertaken, the tax authorities may make a provisional attachment before the tax liability of the taxpayer is finally determined in order to prevent the taxpayer from disposing of his or her properties to avoid payment of taxes.

5. Provisional Security

Indirect taxes such as liquor tax or tobacco tax are collected as a part of sales proceeds by a taxpayer who is entrusted to remit to the government the tax collected.

The tax authorities may require a taxpayer of indirect tax to post provisional security to guarantee payment of the tax in the future. If the taxpayer does not post such security, the tax authorities may secure a hypothecation of the taxpayer's property without the consent of the taxpayer.

21/4 Protection of Taxpayers and Other Persons Concerned

1. Measures for Mitigation

a. Grace of Tax Payment**

When tax payment creates unusual hardships for a taxpayer because of some specific causes, such as illness or damage by natural disaster, the tax

* Provided in the General National Tax Law.

** Stipulated both in the National Tax Collection Law and in the General National Tax Law.

authorities may, upon the taxpayer's request, postpone collection of the tax by no more than one year. In cases where immediate disposal of a taxpayer's properties might endanger his or her business or his or her entire livelihood, or cause him or her unbearable hardships, the tax authorities may at their discretion postpone the sale of properties by no more than one year.

b. Suspension of Execution of Disposition

If there is no property of a delinquent taxpayer to attach or possess, or other circumstances would make collection of national taxes in arrear impossible, the tax authorities may suspend the execution of disposition for delinquent taxes. If the taxpayer's situation remains unchanged at the end of three years, the tax liability is rescinded.

2. Properties Not Subject to Attachment

Properties that are essential to a delinquent taxpayer and his or her dependents to maintain a minimum standard of living or to make their livelihood, or which are an indispensable part of their religious or spiritual life are not subject to attachment. For example, clothes, bedding, furniture, and kitchen utensils indispensable for living cannot be attached, nor can provisions and fuel supplies for three months, or that part of wages or salaries deemed necessary for maintaining minimum standards for the household.

3. Protection of Third Party Rights

When properties are subject to claims by a third party (i.e., a hypothecation or lease), the third party may, under certain conditions, request the tax authorities to attach other properties. The tax authorities are not allowed to immediately attach the movable properties or securities of a delinquent taxpayer possessed by a third person other than those specifically related to the taxpayer. In such a case, when there are no other properties available for attachment, the tax authorities may send the third person a written notice requesting delivery of properties; if the request is not complied with in a specified period, the authorities may proceed to attach such properties.

4. Remedy for Violation of Private Rights

When a taxpayer has an objection with regard to assessment or collection, he or she may, in accordance with the Law concerning Procedures for Administrative Case Litigation and the General National Tax Law, request investigation or reconsideration of the case or bring a lawsuit (for details, see Chapter XIX).

21/5 Time Limits on Assessment and Collection

1. General

The General National Tax Law provides “limitation of actions” on assessment and “prescription” for collection. The meaning of “prescription” as used in this Law conforms to the usual meaning of the term under English law. The term “limitation of actions” refers to the time limitation imposed on tax authorities to make an assessment. This time limit cannot be extended by any action on the part of the tax authorities, as is the case with the prescription period for tax collection (once the tax is assessed).

2. Time Limit on Assessment

a. Ordinary Limit on Assessment

The General National Tax Law provides the following:

- (1) Assessments with respect to national taxes collected under the self assessment system (see **19/1, 2**) must be made within three years (five years for corporation) of the day after the filing deadline, except in cases involving unfiled returns, for which a five-year limit is applicable.
- (2) Assessments with respect to national taxes collected under the official assessment system (see **19/1, 2**) must be made within three years from the date on which tax liability was incurred. If a return of tax base has been filed, however, a five-year limit is applicable.
- (3) In cases involving fraud, assessments with respect to national taxes collected under both the self-assessment system and the official assessment system must be made within seven years of the time limits described in and , as determined by case.

b. Special Rule for Limits on Assessment

The General National Tax Law provides special rules for limits on assessments for the redetermination of taxes in certain situations. Generally, these special situations are limited to such cases as a change in taxable income resulting from court decisions regarding the legality of contracts, or from private agreements affecting performance under contracts which are not permitted under the Commercial and Civil Codes. In such cases, the taxpayer may request an amendment of a tax return within two months of the time when such court decisions or private agreements become effective, and the time limit on assessments mentioned in a. above may be extended on the basis of this date.

3. Extinctive Prescription of Collection

A claim for collection of national tax shall lapse if such a claim is not made within five years after the statutory filing period. In regard to tax evasion, the claim shall lapse if it is not made within five years of the day two years after the due date. Notwithstanding the general principle of prescription provided in the Civil Code, the benefit of extinctive prescription of tax claims is absolute, regardless of whether it is cited. Furthermore, the benefit of extinctive prescription cannot be waived by a taxpayer. Approval, demand, attachment, or request for shares interrupt the prescription for tax purposes.

4. Extinctive Prescription of Refunds

The General National Tax Law also provides time limits on refunds. In order to be accepted, claims for refund must be made within five years of the date such refunds became due.

21/6 Miscellaneous

1. Refund*

When national tax is overpaid as a result of over-assessment, the excess shall be appropriated for any other unpaid national tax. The remainder after this appropriation will be refunded promptly. When the overpaid national tax is refunded or appropriated, interest is paid at the rate of 7.3% per annum from the day following the date of overpayment to the date on which the amount is determined for refund or appropriation. The amount of voluntary payment, however, is governed by different rules. For example, if the refund of overpayment results from a request for corrections, additional refund will be calculated from the date three months after that request, or the date one month after the correction, whichever is earlier.

As for the additional refund rate, there is an exceptional measure such that the rate can be reduced to the standard discount rate determined by Bank of Japan plus 4%.

2. Penalty

If a taxpayer or a third person in possession of properties conceals or destroys properties with the intention of evading payment of national tax claims, he or she shall be imprisoned for no more than three years or fined no more than ¥500,000,

* Stipulated in the General National Tax Law.

or both. A taxpayer who refuses to provide requested information or obstructs questioning or inspection by the tax authorities shall be fined no more than ¥100,000. If a representative of a corporation, etc., has committed the offense, the corporation shall be fined in addition to the punishment of that offender.

3. Interest Tax^{*}

If a taxpayer is permitted by the Tax Office to postpone the payment of tax for a period provided in the Income Tax Law, Inheritance Tax Laws and Special Taxation Measures Law, or to postpone filing a return for a period provided in the Corporation Tax Law and Special Taxation Measures Law, he or she has to pay interest tax for this period instead of delinquent tax. This interest tax is calculated, as a rule, at the rate of 7.3% per annum for income tax and corporation tax and at 6.6%~3.6% per annum for inheritance tax and gift tax, depending on the kind of property acquired.

As for the interest tax rate, there is an exceptional measure such that the rate can be reduced to the official discount rate plus 4%.

^{*} Stipulated in the General National Tax Law.

CHAPTER XXII

TAX DISPUTES

22/1 General

“Appeal of dissatisfaction” and “Litigation” are the systems for examination and remedy in case a person intends to appeal his/her dissatisfaction with his/her reasonable rights and profits being infringed in relation to a national tax.

“Appeal of dissatisfaction” is a system where the person disagreed with the given punishments such as action of correction and attachment can claim against the government office concerned for their cancellation or alteration. First, the relevant person is to insist on his/her dissatisfaction to the administrative office which decided on the punishment. This is what is called an “adverse claim” which occupies a position at the initial stage of an administrative action.

In case the person is dissatisfied even with the decision made in regard to the adverse claim he/she can present a “claim for examination.” Generally, this type of claim should be proposed to the nearest upper administrative office which made the decision. However, the claim for examination with respect to national tax shall be submitted to the head of the National Tax Tribunals established as a third organization for this purpose.

In the event that the relevant person is dissatisfied even with the decision of the National Tax Tribunals, the person can propose litigation to the court.

Number of Cases of Reinvestigation, Reconsideration and Litigation

1. Reinvestigation

(Fiscal Year 2004)

Item	Income Tax Paid by Self- assessment	Income Tax Withheld at Source	Corporation Tax	Inheritance Tax and Gift Tax	Consumption Tax	Tax Collection	Others	Total
Carried over from preceding year	462	36	264	122	266	54	265	1,469
Reinvestigation re- quested	1,682	133	611	463	485	381	517	4,272
Regarded as request for reconsideration	13	4	66	2	45	0	60	190

(Continued)

**Number of Cases of Reinvestigation, Reconsideration and Litigation
(Continued)**

1. Reinvestigation

(Fiscal Year 2004)

Item	Income Tax Paid by Self- assessment	Income Tax Withheld at Source	Corporation Tax	Inheritance Tax and Gift Tax	Consumption Tax	Tax Collection	Others	Total
Number of the cases settled during the year								
Regarded as Withdrawn	6	1	22	1	26	0	26	82
Withdrawn	140	30	72	39	46	80	48	455
Rejected	54	6	24	26	9	162	11	292
Disapproved	1,283	57	370	258	382	149	388	2,887
Partly or wholly canceled	276	28	43	130	66	1	66	610
Modification and others	0	0	0	0	0	0	0	0

2. Reconsideration

(Fiscal Year 2004)

Item	Income Tax Paid by Self- assessment	Income Tax Withheld at Source	Corporation Tax	Inheritance and Gift Tax	Consumption Tax	Tax Collection	Others	Total
Carried over from preceding year	903	47	635	212	443	85	409	2,734
Reconsideration requested	1,124	50	547	235	413	286	432	3,087
Number of the cases settled during the year								
Withdrawn	297	4	84	28	51	41	53	558
Rejected	45	3	16	23	30	99	29	245
Disapproved	803	27	335	183	333	91	314	2,086
Wholly or partly admitted	173	14	118	47	67	3	69	491
Change and others	–	–	–	–	–	2	–	2
Carried over to the next year	709	49	629	166	375	135	376	2,439

Number of Cases of Reinvestigation, Reconsideration and Litigation (Continued)

3. Litigation

(Fiscal Year 2004)

Item	On Tax Assessment								On Tax Collection						Accountant and National Tax Tribunal	Grand Total
	Income Tax	Corporation Tax	Taxes on property	Consumption Tax	Liquor Tax	Other Indirect Tax	Others	Total	Administrative Cases	Suspension of Execution	Compensation for Damages	Other Civil Cases	Easy Cases	Total		
Carried over from preceding year	261	121	67	12	1	—	17	479	24	—	4	22	1	51	4	534
Litigation requested	275	98	52	17	—	—	15	457	41	1	3	44	4	93	2	552
Disposed during the year																
Withdrawn	21	2	3	—	—	—	1	27	4	—	—	17	1	22	2	51
Rejected	7	1	2	—	—	—	1	11	—	1	—	—	—	1	—	12
Disapproved	137	77	47	15	1	—	15	292	31	—	3	17	3	54	3	349
Partly gained	14	2	7	—	—	—	—	23	—	—	—	—	—	—	—	23
Lost	27	2	—	—	—	—	—	31	—	—	—	3	—	3	—	24
Send back	1	—	—	—	—	—	—	1	—	—	—	—	—	—	—	1
Reconciliation	—	—	—	—	—	—	—	—	—	—	—	2	—	2	—	2
Others	1	1	—	—	—	—	—	2	2	—	—	1	1	4	—	6
Total	208	85	61	15	1	—	17	387	37	1	3	40	5	86	5	478
Carried over to next year	328	134	58	14	—	—	15	549	28	0	4	26	0	58	1	608

Note: These tables show the results of reinvestigation, reconsideration, and litigation (only the cases of where the national government is a defendant) on the basis of provisions of tax laws, the Administrative Appellate Law, the Law Concerning Procedure of Administrative Case Litigation and the Law of Civil Procedure.

Source: 130th Annual Statistics Report of the National Tax Agency, 2004.

22/2 Tax Disputes in the Executive Branch

If a taxpayer dissatisfied with the decision made by the superintendent of a taxation office (or the head of the Tax Administration Bureau), the relevant person may claim against the head of the National Tax Tribunals for examination within one month reckoned from the day following the day when a certified copy of the decision made on the objection is delivered.

If no decision is made by the director of a tax office (or the head of the Regional Tax Bureau) even after passage of three months reckoned from the day following the day when the adverse claim is made, a claim for examination may be submitted

Tax Disputes

to the head of the National Tax Tribunals without being given a decision by the director of a tax office (or the head of the Regional Tax Bureau).

However, in the case of ① to ④ of the following items, the relevant person may select to claim for examination without making any adverse claim. In the case of ⑤, no adverse claim may be made, but claim for examination shall be made directly. In such cases, a claim for examination shall be made within two months reckoned from the day following the day when the notice of punishment is received.

- ① In the case of dissatisfaction with a blue return of Income Tax Law or Corporation Tax Law.
- ② In case of dissatisfaction with the final declaration etc prescribed in 130 (1) in the Corporation Tax Law.
- ③ In the case of a punishment decided by the head of the Tax Administration Bureau
- ④ In case no instruction is given to the effect that an adverse claim can be made.
- ⑤ In the case of dissatisfaction with the punishment decided by the head of an administrative organization other than the commissioner or staff of National Tax Agency, Regional Tax Bureau, a tax office or a custom house

(National Tax Tribunals) :

The National Tax Tribunals is an organization to make decisions on claims for examination against legal punishment related to national taxes. In order to contrive remedies respecting the reasonable rights and profits of taxpayers by making appropriate and quick decisions and to help ensure appropriate operation of tax administration, the National Tax Tribunals was established in May, 1970 as an organization attached to the National Tax Agency separated from the offices in charge of imposition and collection of national taxes (tax administration bureaus, taxation offices, etc.). In July, 1984 the National Tax Tribunals was changed from an organization attached to the Tax Administration Bureau to “a special organization.”

(Examination and Decision):

When a claim for examination is submitted and upon submission of a written answer from the body originally in charge of punishment, a consultation body is organized consisting of an examiner in charge and two or more participating judges so that a fair and reasonable conclusion of the matter may be reached. From the viewpoint of establishing a remedy which respects the reasonable rights and profits of the person who claimed for examination, the consultation body shall make intense consultations and conduct sufficient hearings on the assertion of the person concerned to ensure appropriate and quick investigation and examination.

Based on the resolution of the consultation body, the head of the National Tax Tribunals may reject claims without due reason and cancel or change the punishment or a part whereof if there is a due reason. However, the head cannot change the punishment in a case where such change might disadvantage the person who claimed for examination. In case the claim for examination is made after the passage of the legal period, or in case the claim itself is illegal, the head shall make a decision to reject it. The decision made by the head of the National Tax Tribunals shall be considered as the final determination of the Administration Bureau and, consequently, no appeal may be proposed by the government office in charge of the initial punishment even if it is dissatisfied with the decision.

22/3 Tax Dispute in the Judicial Branch

Litigation is a system for a court as an independent and fair third party to solve disputes in accordance with the oral pleas of the parties concerned which are opposed to each other, and it occupies the most important rank in protecting the nation's rights and profits.

In Japan, litigation on administrative cases is also examined by a Court of Justice, and no court of administration is established. Litigation to claim for cancellation of imposition and collection of taxes can be proposed only after a decision or judgment is made on the appeal of dissatisfaction in principle. The litigation for cancellation shall be proposed within six months in principle reckoned from the date when the fact that judgment has been made against the claim for examination is announced.

Even upon presentation of litigation, the punishment over which the dispute has arisen will remain effective till cancellation of the judgment is settled.

CHAPTER XXIII

LOCAL TAXES

23/1 Local Public Entity

1. Legal Foundation

Japan, which is not a federated state but a single sovereign state, has a long tradition of local autonomy. The Constitution of 1947 assures a high degree of local autonomy. Its chapter on Local Self-Government reads as follows:

Article 92. Regulations concerning organization and operation of local public entities shall be fixed by law in accordance with the principle of local autonomy.

Article 93. Local public entities shall establish assemblies as their deliberative organs, in accordance with the law. The chief executive officers of all local public entities, the members of their assemblies, and other such local officials as may be determined by law shall be elected by direct popular vote within their communities.

Article 94. Local public entities shall have the right to manage their property, affairs, and administration and to enact their own regulations within the scope of the law.

Article 95. A special law, applicable only to one local public entity, cannot be enacted by the Diet without the consent of a majority of the voters of the local entity concerned, obtained in accordance with the law.

On the basis of provisions as set forth in the Constitution, the following laws have been instituted as fundamental laws for the local finance system:

The Local Autonomy Law (17 April 1947; Law No. 67)

The Local Finance Law (7 July 1948; Law No. 109)

The Local Tax Law (31 July 1950; Law No. 226)

2. Kinds of Local Organizations

Local public entities consist of municipalities (cities, towns, and villages) that are primary, basic local organizations and prefectures that are larger units but secondary local organizations.

3. Prefectures

Forty-seven prefectures are divided into the following four categories:

To (Metropolis) Tokyo

Do (Circuit) Hokkaido

Fu (Prefecture) Osaka and Kyoto

Ken (Prefecture) 43

Densely populated areas of the Tokyo Metropolis are sub-divided into 23 special wards, whereas prefectures have cities, towns, and villages. A special ward is not a completely independent public entity but is, in some respects a subdivision of the Metropolitan administration. The 23 special wards, therefore, come under its administrative jurisdiction in certain administrative areas. On the other hand, there are no fundamental differences between circuits and prefectures.

Of the circuits and prefectures, the largest is Hokkaido, with an area of 83,452 square kilometers and the smallest is Kagawa Prefecture, with an area of 1,875 square kilometers.

In terms of population, Tokyo Metropolis is the largest entity, with 12,586,642 persons while the smallest prefecture is Tottori Prefecture, with 603,936 citizens (Estimates of March 31, 2006). The chief executive of the prefecture is the governor and its legislative body is the assembly. The governor and members of the assembly are directly elected for a term of four years. Prefectures are responsible for the police force, public works such as construction of roads and waterways, public health, social welfare, labor administration, high schools and other higher education, libraries, and public housing.

4. Municipalities

The number of cities, towns, and villages is as follows:

	(as of March 31, 2006)
Cities	777
Towns & Villages	1,044
Total	1,821

In the 1950s, there were about 10,000 cities, towns, and villages, many of which were too small to be capable of effectively administering their own affairs. As a result of the merger of municipalities that was encouraged by the government, the number has decreased substantially.

The chief executive of a city, town, or village is the mayor or the head of such entities. The legislative body is the assembly. The mayor and members of the assembly are directly elected for a term of four years. The main financial responsibilities of a city, town, or village include elementary and junior high school education; public works such as the construction of roads and parks; sewage and disposal of human waste and trash; fire prevention and firefighting; unemployment relief; public health insurance and; the administration of national pensions and ports and harbors.

23/2 Local Public Finance System

1. Local Revenue Structure

The revenue of local public entities consists of local taxes, local transfer taxes, special Local grants, local allocation taxes, national expenditures, public bonds, fees and charges and miscellaneous revenue. According to the local public finance plan for fiscal year 2006 the sources of revenue are:

	Amount	(in billions of yen)	(%)
Local Taxes	34,898		42.0
Local Transfer Tax	3,732		4.5
Special Local Allocation	816		1.0
Local Allocation Taxes	15,907		19.1
National Subsidies	10,202		12.2
Public Bonds	10,817		13.0
Fees and Charges	1,645		2.0
Miscellaneous 1	5,133		6.2
Total	83,151		100.0

Of these items, Local Transfer Taxes, Special Local Allocation, Local Allocation Taxes, and National Subsidies are granted from the National Treasury to local public entities. Hence, about 40% of the revenue of local public entities is provided by the national government.

2. Local Taxes

The Local Tax Law provides for taxes to be levied by local public entities and prescribes the basis of tax calculation and collection for each tax. It also provides standard tax rates to be used by local public entities. For several taxes, however, the local public entity may, when necessary, levy taxes exceeding standard tax rates but subject to the limits set by the Local Tax Law.

Local public entities can establish new tax items in addition to those specified as local tax items. The new tax items shall include general tax not stipulated in Local Tax Law whose revenue sources are specified and object tax not stipulated in Local Tax Law whose uses are specified. In establishing these tax items, approval should be obtained from the Minister for Internal Affairs and Communications. The Minister for Internal Affairs and Communications shall give the approval unless the relevant case falls under either of the following categories:

- (1) Burdens to residents would be exceedingly heavy since standard of imposition of such additional taxes are the same as those of the national and other local taxes.
- (2) Serious hindrance might be given to physical distribution among local bod-

ies.

- (3) Such additional taxes are considered as inappropriate in the light of the national economic policy.

Prefectures, cities, towns, and villages levy and collect their own taxes respectively. Note that the national tax authority collects the local transfer tax, etc. and distributes it among local public entities according to a certain standard.

The prefectural individual inhabitants tax is collected by municipalities along with the latter's individual inhabitants tax. The local consumption tax is collected by the National Government though it is prefectural tax in order to lighten the burden of taxpayers.

3. Local Transfer Tax

The local transfer tax consists of the local road tax, liquefied petroleum gas transfer tax, motor vehicle tonnage transfer tax, aviation fuel transfer tax, special tonnage dues and Income Transfer Tax.

Local road tax is imposed on gasoline consumption and is collected together with the national gasoline tax for administrative convenience. Like the gasoline tax, the local road tax is a tax earmarked specifically for road expenditures. Since the local road tax is collected largely in areas where petroleum refineries are located and is intended for road expenditures throughout the country, 43% of this revenue is distributed among prefectures and the fifteen largest cities, which are to take care of the roads within their own city limits, taking into account the extension and size of their roads. The remaining 57% of the revenue is distributed among other cities, towns, and villages.

The local road tax is ¥5,200 per kilolitre, compared to the national petroleum tax of ¥48,600 per kilolitre (see Chapters XI and XVI).

The liquefied petroleum gas transfer tax is distributed by the National Government. One-half of the national tax revenue from the liquefied petroleum gas tax is allocated to prefectures and the fifteen largest cities for road expenditures (see Chapter XII).

The motor vehicle tonnage transfer tax is distributed by the National Government among cities, towns, and villages for road expenditures. One-third of the total motor vehicle tonnage tax revenue is earmarked for construction and improvement of local roads (see Chapter XVII).

The aviation fuel transfer tax is distributed by the national government among prefectures, cities, towns, and villages concerned for the prevention of disturbances caused by aircraft noise and for the improvement of airports and their vicinities. The amount so distributed is two-thirteenths of the revenue from the aviation fuel tax (see Chapter XIII). One-fifth of this amount is distributed among

prefectures and the remaining four-fifths among cities, towns, and villages.

Special tonnage dues are collected by the national government together with the national tonnage dues from ocean-going vessels entering Japanese ports. They are given to cities, towns, and villages that are responsible for the administration of ports and harbors. The rate for special tonnage dues is ¥20 per tonne upon each entry; if paid annually instead of upon each entry, it is ¥60 per tonne for one year.

The purpose of the Income Transfer Tax is to transfer a portion of national tax revenues to local governments as general revenue for unspecified uses, and it is a tentative measure until the national government transfers the sources of tax revenue to the local governments. Of the revenue from the income tax, 3,009.4 billion yen is transferred in FY2006. 2,179.4 billion yen of which is transferred to prefectural governments and 830.0 billion of which is transferred to municipal governments, based on the tax rate of individual inhabitant taxes levied after the transfer of sources of tax revenue (prefectural tax: 4%, municipal tax: 6%). (In conformity with the full-scale transfer of sources of tax revenue, from income tax to individual inhabitant tax in FY2007, the Income Transfer Tax will be abolished after FY2006.)

4. Special Local Allocation

The special local grant, consisting of the special grant for tax reduction compensation and the special grant for child benefit shall be delivered to prefectural and municipal governments and special wards of Japan whether or not local allocation tax is delivered.

The special grant for tax reduction compensation is to be delivered for the time being as a financial source alternative to the local tax in order to compensate part of the losses, which accompanied the permanent reduction in taxes in 1999. The total grant shall be the amount obtained by subtracting the increase in revenues from the local tobacco tax, resulting from changes in the national and local rates of tobacco tax and the amount of supplement to make up for the increase (3.8%) in the tax rate of local grants for corporation taxes from three-quarters of the total estimated decrease in the incomes for individual fiscal years resulting from permanent tax reduction.

To lessen the economic burden on child-rearing households, the age eligible to receive child allowance was raised from “having completed the third year of elementary school” to “having completed elementary school,” and parents’ income eligible was also raised at the same time. The national government transfers a half of the costs of these expansions as the special grant for child benefit to the prefectural and municipal governments respectively, to meet the increased

financial burden of the local governments. (The special grant for the planned transfer of sources of tax revenue was abolished in FY2006, because all of the transfer of sources of tax revenue, which was mentioned on the reform of national subsidies, is made by Income Transfer Tax.)

5. Local Allocation Tax

Local Allocation Tax is granted to local public entities for unspecified uses so that they may fulfill their own duties to the fullest extent while solving the disparity in financial resources and indemnifying them for the amount that will not go toward their total revenue. Local allocation tax has the same characteristics as the general grant in the United Kingdom and the adjustment grant in Germany. However, the system of local allocation tax is more comprehensive and complicated.

Local Allocation Tax is 32.0% of the income tax and liquor tax; 35.8% of corporation tax, 29.5% of consumption tax, and 25.0% of tobacco tax which together comprise 27.5% of all of the national general accounts' tax revenue in the FY 2006 budget.

As mentioned, the total amount of the Local Allocation Tax is generally linked to the revenue of five national taxes. However, recent shortage of financial resources suffered by local entities has led the National Government to address the problem such as an increase in the Local Allocation Tax as part of a package of local financial measures.

The total amount of the Local Allocation Tax in FY2006 is ¥15,907 billion yen, which breaks down into ¥13,743 billion in Local Allocation Tax Allocation from the General Account to the Special Account for Allocation Tax and Transfer Tax Dividend, ¥470 billion surplus, ¥1,081 billion in borrowing funds from the Special Account above mentioned and ¥1,291 billion carried over from preceding year minus ¥677 billion in interest on borrowing funds.

Local Allocation Tax consists of two parts—94% of which is the ordinary allocation tax and the remaining 6% of which is a special allocation tax. Ordinary grant tax is given to each local public entity in accordance with the difference between the amount of basic financial needs and the basic financial revenue. Each local public entity receives an amount equal to this difference.

6. National Subsidies

Subsidies from the national government are grants, charges, supplementary money, and other funds given to local public entities after the purposes for their disbursement are designated by the government. They cover a wide range of fields such as public works, social security, and education.

7. Local Public Bonds

Local public entities are not authorized to issue bonds for the purpose of raising revenue except in limited cases; namely, to procure funds for public works, etc.

A local public entity desiring to issue such loans needs authorization from the Minister for Internal Affairs and Communications, or the Governor of the prefecture.

One of the main fund sources to absorb such loan issues is the Fund of the Government which receives funds mainly from postal savings. Besides these sources, loans from private banking institutions and the Japan Finance Corporation for Public Enterprises (JFM) are also used for accepting such local government bonds.

8. Miscellaneous Revenues, etc.

Included in miscellaneous revenues, etc. are various charges or fees, revenue from the disposition of properties, donations, etc.

23/3 Prefectural Taxes

1. Prefectural Inhabitants Tax

a. Taxpayers

Individual Inhabitants Tax is levied on individuals residing in a prefecture and having income in the past year. It consists of taxes on a per capita basis, income basis, interest basis, dividend basis, and basis of capital gains from transfer of stocks.

Whether an individual maintains a domicile in a prefecture is ascertained as of 1 January each year.

Corporation Inhabitants tax is levied on a corporation having its office or place of business in a prefecture on a per capita basis and interest basis, as well as on a tax amount of the national corporation tax. The per capita tax is levied on a corporation that does not have its office in the prefecture but which has a dormitory, etc., there.

b. Tax Base and Tax Rates

The standard rate for the per capita tax for individuals is ¥1,000 per person per annum.

Standard tax rates on individual income are as follows:

For Taxable income of ¥7,000,000 or less 2%
--	----------

over ¥7,000,000 3%

Note) Standard tax rate is uniformly 4% after FY2007 along with the transfer of tax revenue from the National income tax to the Local inhabitants tax.

The tax rate on an interest basis on individuals and corporations is 5%. The tax rate on a dividend basis on individuals is 5%. Provided, however, that the rate of taxation on special dividends, etc., to be paid during the period from January 1, 2004, to March 31, 2008, is 3%.

The tax rate on a basis of capital gains from transfer of stocks on individuals is 5%. Provided, however, that the rate of taxation during the period from January 1, 2004 to December 31, 2007 is 3%.

The taxable income for individuals is the same as for the municipal inhabitants tax (see 23/4,1.b.(1)).

Separate tax treatment is provided for forest income, retirement income and capital gains from transfer of land, buildings and the rights to land, business income, capital gains and miscellaneous income from transfer of stocks, and business income and miscellaneous income from futures transactions. In addition, deductions, as is the case with income tax, are allowed on business income for taxpayers filing blue returns.

Per capita tax rates for corporations are as follows:

	Standard rate
Corporations with capital plus reserve funds of more than ¥5,000 million	¥800,000
Corporations with capital plus reserve funds of more than ¥1,000 million but not more than ¥5,000 million	¥540,000
Corporations with capital plus reserve fund of more than ¥100 million but not more than ¥1,000 million	¥130,000
Corporations with capital plus reserve funds of more than ¥10 million but not more than ¥100 million	¥50,000
Other corporations	¥20,000

The standard tax rate on a tax amount for the national corporation tax is usually 5.0%.

The prefecture can levy tax above this rate but no more than 6.0%.

c. Time of Payment and Collection

As with municipal tax, individuals generally pay prefectural tax in four installments—June, August, October, and January of the following year. The tax

is paid to municipalities together with the municipal inhabitants tax. The municipalities then remit the prefectural tax to the prefecture. For wage earners, payment is made by withholding (a special collection system) under the same system that applies to municipal tax.

For a corporation, payment should generally be made within two months of the close of the accounting period. If a corporation has offices or places of business in two or more prefectures, the tax amount is divided by prorating the total tax on the basis of the number of employees in each office and paid based on its returns.

2. Enterprise Tax^{*}

a. Taxpayers

Enterprise tax is levied on (1) corporations engaged in business and having an office or place of business in the prefectures, and (2) individuals engaged in a prescribed type^{**} of business or profession as set forth in the Law.

Corporations or individuals engaged in businesses such as forestry and mining of mineral ores are exempt from the tax.

The enterprise tax is not levied on individuals engaged in farming nor those engaged in fishing operations chiefly through their own or their family's labor.

b. Tax Base and Tax Rates

(1) Corporations

^{*} The nature of Enterprise Tax is explained below:

Though the tax base of Enterprise Tax is either income or gross receipts of an enterprise, the nature of the tax is one imposed on business activities, not on income.

In order to carry on business profit-making activities, an enterprise uses various prefectural services such as road construction or maintenance, port facilities, health services, air pollution control, water supply for industrial use, etc.

Thus, Enterprise Tax is deemed to be a kind of contribution from enterprises to the prefecture for these services.

Therefore, Enterprise Tax should be based on criteria that shall be commensurate with the scale of business activities.

However, most enterprises are subject to Enterprise Tax on the basis of their income.

This is based on two reasons:

First, the amount of business income can be an indirect indication to allow tax authorities to infer the scale of business activities that took place during a taxable period.

Second, if tax authorities use a tax base that is the same as that of Income Tax or Corporation Tax, burdens on taxpayers as well as those for tax authorities could be reduced.

For these two reasons, enterprises other than electric supply industries, gas supply industries, and insurance companies are subject to Enterprise Tax on the basis of their income, which is also used as the tax base for the Corporation Tax.

^{**} Prescribed types of businesses are divided into the following three categories:

Category I :	Retail and wholesale, finance, manufacturing, transportation, warehouses, printing, publishing, photo studios, hotels or inns, restaurants or coffee houses, public entertainment, recreation houses, agents, etc.
Category II :	Livestock industry (excluding that which is subordinate to agriculture), fishery, etc., other than businesses involved in capturing small marine products.
Category III :	Medical professionals, dentists, pharmacists, midwives, masseurs, farriers, horse-shoers, lawyers, certified tax accountants and other accountants, patent attorneys, judicial scriveners, land surveyors, barbers, beauty parlors, laundries, etc.

In principle, business income and income upon liquidation are the basis for levying the corporation enterprise tax. Computation of income is almost the same as that for the national corporation tax. The scope of taxable income is, for corporation enterprise tax purposes, however, narrowly defined in some respects and more widely in others, compared to the national corporation tax, reflecting the characteristics of the enterprise tax as one closely linked to the benefits given by local governments. For example:

- ① Special measures regarding non-deductibility of reserves.
- ② Special measures regarding deductibility of loss that is carried over.
- ③ Special measures regarding income calculation of corporations that deduct tax amounts of individual income tax from their income.
- ④ Special measures regarding the upper limit of deductibility of donations.
- ⑤ Special measures regarding the deductibility of foreign tax of domestic corporations.
- ⑥ Special measures regarding the consultation fee of medical corporations.
- ⑦ Special measures regarding the calculation of suspended income of fishery cooperatives, etc.

Standard tax rates applicable to ordinary corporations are as follows:

For annual income of no more than ¥4,000,000	5%
over ¥4,000,000 yen but no more than ¥8,000,000	7.3%
over ¥8,000,000	9.6%

Standard tax rates applicable to cooperative associations, etc., are as follows:

For annual income of no more than ¥4,000,000	5%
over ¥4,000,000	6.6%

The definition of special corporations, etc., for enterprise tax purposes is almost the same as that for national corporation tax purposes (see 3/2, 1. a).

Reduced rates of 5% and 7.3% listed above are not applicable to corporations and cooperative associations with offices in more than three prefectures and capital of no less than ¥10 million.

The corporation tax base of a company whose capital or investment is in excess of ¥100 million (excluding nonprofit foundations or special corporations) shall be the total of the income levy, added value levy and capital levy.

(1) Tax base

- (a) Income levy: Incomes and liquidation incomes
- (b) Added value levy: Amount of added values

(Compensations/wages + net interest paid + net rent paid \pm profits

and losses in a single fiscal year)

In case the amount of compensations/wages accounts for more than 70% of the returns distributed (compensations/wages + net interest paid + net rent paid), the amount in excess shall be deducted from the amount of added values.

(c) Capital levy: Amount of capital (Amount of capital or investment + amount of capital reserved or consolidated capital reserved)

For a certain holding company, the amount obtained by multiplying the capital by the rate of the booked values of the stocks of its subsidiaries against the total assets shall be deducted.

In the case of a corporation whose capital is in excess of ¥100 billion, the amount obtained by multiplying the rate decided in accordance with the capital divisions stated below plus ¥100 billion shall be the tax base of the capital levy.

However, in the case of the corporation whose capital amount is in excess of ¥1 trillion, the capital amount shall be considered as ¥1 trillion.

A: The part from more than ¥100 billion to
¥500 billion or less: 50%

B: The part from more than ¥500 billion to
¥1 trillion or less: 25%

(2) Tax Rate

(a) Income Levy:

Annual income: ¥4 million or less:	3.8%
From more than ¥4 million to ¥8 million or less:	5.5%
More than ¥8 million:	7.2%

(b) Added value levy: 0.48%

(c) Capital levy 0.2%

(3) Grace period

A grace period of a maximum of six years is allowed for a corporation whose business shows losses for more than three years or a deficit venture firm whose period of operation is less than five years from its foundation.

An exception to the general principle, gross receipts, instead of income, are used as the basis of assessment for the enterprise tax levied on electricity corporations, gas corporations, and insurance corporations. In the case of electric power and gas corporations, however, revenues raised independently of the regular business, such as receipts from the sale of fixed assets or securities, insurance money receivable, government sub-

sidies, etc., are not included in “gross receipts” for enterprise tax purposes. “Gross receipts” of insurance corporations are obtained by applying specified percentages to net premiums receivable (insurance premiums receivable less reinsurance premiums payable). Standard tax rate of 1.3% is applicable to such gross receipts.

Prefectures may raise the tax rate up to 1.2 times the standard tax rate according to their financial needs.

(2) Individuals

As for individual taxpayers, the enterprise tax is levied in the fiscal year beginning 1 April on income derived during the previous calendar year. Income is computed by deducting necessary expenses from gross receipts.

This generally conforms to the calculation of business income or real estate income as the basis of assessment for income tax purposes.

However, as in the case of corporations, taxable income is narrowly defined in some respects and widely defined in others, compared to the national income tax calculation. For example, the special deduction for overseas transactions of technical services is not granted.

Although deductions and exemptions allowed under the Income Tax Law are not applicable in computing taxable income for the enterprise tax, taxpayers are entitled to a fixed deduction of ¥2,900,000 (called “proprietor deduction”).

Standard tax rates applicable to individuals vary according to the type of business as follows:

(a) Category I	5%
(b) Category II	4%
(c) Category III (other than (d) below)	5%
(d) Category III (masseur, midwife, farrier, etc.)	3%

Prefectures may raise the tax rate up to 1.1 times the standard tax rate according to their financial needs.

c. Payment

Corporate enterprise tax is generally paid by self-assessment within two months from the closing day of the accounting period (see 3/5.). Corporations with an accounting period exceeding six months are required to file an interim return in the two months after the end of the first six months of the period.

For an individual, enterprise tax is assessed on the basis of reported (corrected or determined) business income or real estate income for national income tax. Payment is made in two installments, usually in August and November.

As for corporate enterprise tax, those having offices in two or more pre-

fectures must pay taxes to the respective prefectures where the offices are located. In such a case, tax is determined, as a rule, by allocating the total tax to the various places of business on the basis of the number of employees at each location and the number of locations for non-manufacturing industry and the number of employees at each location for manufacturing industry. There are, however, some exceptions. For example, electric power and gas utilities apportion their earnings on the basis of the value of fixed assets, while railways divide their income proportionally to the length of track.

3. Local Consumption Tax

a. General

The Local Consumption Tax (prefectural tax) was established on April 1, 1997 to replace Consumption Transfer Tax.

b. Taxpayer

A taxpayer of the Consumption Tax

c. Tax Base

- (1) For domestic transactions, the tax base is the amount for the Consumption Tax.
- (2) For import transactions, the tax base is the amount for the Consumption Tax levied on the receipt of taxable cargoes from bonded areas.

d. Tax Rate

Tax rate is 25% of the consumption tax amount (equivalent to consumption tax rate of 1%)

e. Assessment and Payment

- (1) The enterprises that are subject to file a final return must file a final return with that of Consumption Tax and pay the declared Local Consumption Tax amount with the Consumption Tax amount by the deadline for the declaration of Consumption Tax.
- (2) Those who receive taxable cargoes from bonded areas must file a fixed return with that for the Consumption Tax to the Director-General of Customs and pay the declared Local Consumption Tax amount with the Consumption Tax amount.

[Note 1] The enterprises declare and pay Local Consumption Tax using the same return and tax payment slip as with Consumption Tax.

[Note 2] While Local Consumption Tax is a Prefectural Tax, the state

executes this tax with the Consumption Tax considering the burden or taxpayers, etc.

4. Real Property Acquisition Tax

a. Taxpayers

This tax is paid by person acquiring land or houses. This does not apply to land or houses acquired through inheritance or the merger or division of corporations.

b. Tax Base and Tax Rates

The basis of assessment is the appraised value of the land or houses at the time of acquisition. The tax rate is 4% (3% for the houses and lands acquired between April 1, 2006 and March 31, 2009. 3.5% for the buildings other than house acquired between April 1, 2006 and March 31, 2008.) .

When a new house, with floor space no more than 240 square meters and no less than 50 square meters (40 square meters for a rented apartment, etc.) is built for residential purposes, a deduction of ¥12,000,000 from the appraised value of the house is allowed.

If a residential house that is pursuant to this special deduction is built within three years of or one year before acquisition of the site, the tax levied on the appraised acquisition value of the site is reduced by 3% of ¥1,500,000 or 3% of the value of a site that has twice as much floor space (up to 200 square meters), whichever is higher.

The above special deduction for newly built houses also applies to cases where the owner has acquired a second-hand home.

In such cases, the amount of the decided by its value at the time of foundation.

The tax shall be exempted when the appraised value of the land or house is below the following amounts:

For land	¥100,000
For a new house	¥230,000
For any other house	¥120,000

As for the residential land, etc. acquired between Jan. 1, 2006 and Dec. 31, 2009, the basis of assessment is reduced to one-half of its appraised value.

c. Payment

Prefectures make assessments based on a report of the person who acquired real estate. The time of payment is provided for in prefectural ordinances.

5. Tobacco Tax**a. Taxpayer**

Persons who produce tobacco or wholesale it.

b. Tax Base

The quantity of cigarettes.

c. Tax Rates

Prefectural tobacco tax ¥1,074 per thousand cigarettes

Municipal tobacco tax ¥3,298 per thousand cigarettes

d. Payment

The tax on sales in a month is due by the end of the following month.

6. Golf Course Utilization Tax**a. Taxpayers**

Persons who use golf courses.

b. Tax Base and Tax Rates

The standard tax rate is ¥800 per day per player and cannot be over ¥1,200 per day per player.

c. Payment

Operators of golf courses specially collect the tax and make payment.

7. Automobile Tax**a. Taxpayers**

Persons owning vehicles registered in a prefecture.

b. Tax Base and Tax Rates

Standard annual tax rate is determined by the type of vehicle.

Passenger cars:

Cars with a cylinder volume of:

		commercial use	non-commercial use
Over	But not over		
6,000cc		¥40,700	¥111,000
4,500cc	6,000cc	¥27,200	¥88,000
4,000cc	4,500cc	¥23,600	¥76,500
3,500cc	4,000cc	¥20,500	¥66,500

XXIII Local Taxes

3,000cc	3,500cc	¥17,900	¥58,000
2,500cc	3,000cc	¥15,700	¥51,000
2,000cc	2,500cc	¥13,800	¥45,000
1,500cc	2,000cc	¥9,500	¥39,500
1,000cc	1,500cc	¥8,500	¥34,500
	1,000cc	¥7,500	¥29,500

Trucks:

(Tax base for trucks whose loading capacity is over 4 tonne and not more than 5 tonne)

Commercial use	¥18,500
Non-commercial use	¥25,500

Buses:

(Tax base for buses whose riding capacity is over 40 and less than 50 passengers)

Commercial use:	
For ordinary passengers	¥17,500
Others	¥38,000
Non-commercial use:	¥49,000

Three-wheeled small cars:

Commercial use:	¥4,500
Non-commercial use:	¥6,000

c. Payment

The tax is generally levied at the full annual rate on vehicles registered as of 1 April every fiscal year. In principle, payment is made in May. When vehicle registrations are made during the course of a fiscal year, the owner of the vehicle is taxed for the remaining period of that fiscal year. In this case the tax is reduced proportionately for the number of months elapsed.

8. Automobile Acquisition Tax

This tax was established in FY1968. It is designed to meet expenditures required for prefectural and municipal roads. Prefectural governments transfer to municipal governments 70% of the tax revenue on the basis of the area and distance of municipal roads.

a. Taxpayers

The tax is paid by persons acquiring an automobile. In the event an automobile is sold with its title reserved by the seller, then the purchaser must pay the tax.

An automobile, is one which is provided for in the Vehicles for Road

XXIII Local Taxes

Transportation Law but excludes certain special automobiles and two-wheeled automobiles falling under the category of motorcycles or light automobiles. No tax is levied on the acquisition of an automobile by the National Government or local public entities or on acquisition through inheritance or through the merging or dividing of corporations.

b. Tax Base and Tax Rate

The tax is assessed on the basis of the price paid for the automobile. But if the automobile is acquired free of charge, then it is on the basis of the value involved in a normal transaction. The tax rate is fixed at 3% (5% for noncommercial motor vehicles except for light motor vehicles, acquired for private use from 1 April 1974 to 31 March 2008); an automobile purchased at ¥500,000 or less is exempt from this tax.

c. Payment

The tax must be declared and paid on a self-assessment basis by the following dates:

- (1) For an automobile to be registered for the first time or with use reported;
The date when such registration or report is made.
- (2) For an automobile undergoing transfer that will be registered;
Within 15 days of the transfer.
- (3) For an automobile other than those above;
Within 15 days of acquisition.

In declaring, certificate stamp needs to be stamped on the report.

9. Mine-lot Tax

a. Taxpayers

Persons possessing mining rights.

b. Tax Base and Tax Rates

Ore deposit mining: ¥200 per annum per hectare (10,000 m²)

Other mining area: ¥200 per annum per hectare for mines being prospected
and ¥400 per hectare for mines in operation.

In the case of a mine-lot of oil or combustible natural gas, the tax rate is reduced by one-third of the above. Ore deposit mining area existing on shores along the rivers; ¥600 for extension of 1,000 m each

c. Payment

Assessed by prefectures. Collected generally in May.

10. Hunting Tax

Revenue from this tax is used only for the protection of birds and animals or for the administration of hunting.

a. Taxpayers

Registered hunters

b. Tax rate

¥16,500 or ¥11,000 or ¥5,500 per each prefecture where hunting registration is rendered depending on the type of hunting license.

c. Payment

Assessed by prefectures. Payment based on regulations.

11. Light-Oil Delivery Tax

Revenue derived from this tax must be used by the local authorities for road projects. As explained previously, the fifteen largest cities are responsible for the maintenance of roads within their own city limits. Therefore, prefectures where these fifteen cities are located transfer 90% of the light-oil tax revenue to those cities concerned based on the total area etc. of their roads.

a. Taxpayers

Persons receiving light-oil from a refiner, an importer, or a wholesaler under special contract with a refiner.

Since the aim of the tax is to raise funds for roads, light-oil used for industries having no connection with roads is exempt from the tax. Such are the cases for light-oil used for heating boats and the generation of electricity.

b. Tax Base and Tax Rate

Its tax rate is fixed at ¥15,000 per kilolitre. However, the rate is ¥32,100 per kilolitre until 31 March 2008.

c. Payment

Vendors specially collect the tax together with the charge for light-oil. The tax collected for the month is paid by the end of the following month.

12. Other Taxes

(1) General and Object tax not stipulated in Local Tax Law

In Prefectures listed below, taxes other than those provided in Local Tax

Law are established subject to obtaining approval from the Minister for Internal Affairs and Communications.

Nuclear-fuel tax is imposed in Hokkaido, Aomori, Miyagi, Fukushima, Ibaraki, Niigata, Ishikawa, Fukui, Shizuoka, Shimane, Ehime, Saga and Kagoshima prefectures. While special tax on gasoline is imposed in Okinawa prefecture, accommodation tax is imposed in Tokyo Metropolis. Hokkaido, Aomori, Iwate, Miyagi, Akita, Yamagata, Fukushima, Niigata, Mie, Aichi, Shiga, Kyoto, Nara, Okayama, Hiroshima, Tottori, Shimane, Yamaguchi, Fukuoka, Saga, Nagasaki, Kumamoto, Oita, Miyazaki, Kagoshima and Okinawa prefecture impose Industrial-Waste Tax. etc. Norikura Environmental-Preservation Tax is imposed in Gifu prefecture and Temporary special cooperate Tax is imposed in Kanagawa.

(2) Others

Water and Land Utilization tax is another tax item established by prefectures.

23/4 Municipal Taxes

1. Municipal Inhabitants Tax

a. Taxpayers

Same as for the prefectural inhabitants tax.

b. Tax Base and Tax Rate

(1) Individuals

(a) General

Taxable income for the inhabitants tax is obtained by deducting the exemptions and exemptions described below from the total of ordinary income, retirement income*, and timber income, in the previous year, which are computed in almost the same method as provided under the Income Tax Law. As mentioned in (b) below, specific capital gains are, or maybe, taxed separately.

(i) Deductions for casualty losses and medical expenses

The maximum deductible amount is computed in the same way as national income tax (see 2/4, 1 and 2). However, since the taxable income is not entirely the same as for income tax, the deductible amount varies slightly.

* Since 1967, retirement income has been subject to prefectural and municipal inhabitants taxes in the year in which it is paid and is taxed separately from other income.

Taxable retirement income is computed in the same way as income tax (see 2/3, 2. (6)).

Tax rates are the same as the standard rates for prefectural and municipal inhabitants taxes.

- (ii) Deduction for social insurance premiums
The amount of social insurance premiums paid.
- (iii) Deduction for small-scale enterprise mutual aid premiums
The total amount of small-scale enterprise mutual aid premiums.
Premiums for personal pensioners in accordance with Defined Contribution Pension Law and Mutual aid premiums for mentally and physically handicapped persons.
- (iv) Deduction for life insurance premiums
 - 1. When the entire premium is for life insurance, the following may be deducted:
 - (1) When the amount of the paid premium is under ¥15,000. . . . the amount of the paid premium
 - (2) When the amount of the paid premium is over ¥15,000 and under ¥40,000. . . . $\text{¥7,500} + 1/2 \times [\text{the amount of the paid premium}]$
 - (3) When the amount of the paid premium is over ¥40,000 and under ¥70,000. . . . $\text{¥17,500} + 1/4 \times [\text{the amount of the paid premium}]$
 - (4) When the amount of the paid premium is over ¥70,000. . . . ¥35,000
 - 2. When the entire premium is for an individual pension plan
 - (1) When the amount of the paid premium is under ¥15,000. . . . the amount of the paid premium
 - (2) When the amount of the paid premium is over ¥15,000 and under ¥40,000. . . . $\text{¥7,500} + 1/2 \times [\text{the amount of the paid premium}]$
 - (3) When the amount of the paid premium is over ¥40,000 and under ¥70,000. . . . $\text{¥17,500} + 1/4 \times [\text{the amount of the paid premium}]$
 - (4) When the amount of the paid premium is over ¥70,000. . . . ¥35,000
 - 3. When the premium is for both a life insurance and an individual pension plan. . . . $[\text{the amount calculated under the disposition of 1. regarding life insurance}] + [\text{the amount calculated under the disposition of 2. regarding an individual pension plan}]$
- (v) Deduction for Casualty Insurance Premiums
 - 1. When the entire premium is for short-term fire and other casualty insurance
 - (1) When the amount of the paid premium is under ¥1,000. . . .the amount of the paid premium

XXIII Local Taxes

- (2) When the amount of the paid premium is over ¥1,000 and under ¥3,000. . . ¥1,000 + $\frac{1}{2} \times (\text{the amount of the paid premium} - ¥1,000)$
 - (3) When the amount of the paid premium is over ¥3,000. . . . ¥2,000
 2. When the entire premium is for long-term fire and other casualty insurance
 - (1) When the amount of the paid premium is under ¥5,000. . . . the amount of the paid premium
 - (2) When the amount of the paid premium is over ¥5,000 and under ¥15,000. . . ¥5,000 + $\frac{1}{2} \times (\text{the amount of the paid premium} - ¥5,000)$
 - (3) When the amount of the paid premium is over ¥15,000. . . . ¥10,000
 3. When the premium is for both short-term and long-term fire and other casualty insurance
 - (1) When the amount calculated under the disposition of 1. and 2. is under ¥10,000. . . . the amount calculated under the disposition of 1. and 2.
 - (2) When the amount calculated under the disposition of 1. and 2. is over ¥10,000. . . . ¥10,000
- Note) Deduction for insurance premium is revamped to the “deduction for earthquake insurance premium” in individual inhabitants tax in FY2008.
- (vi) Exemption for the handicapped
- If a taxpayer is handicapped or has a handicapped spouse or dependent relative ¥260,000
- If severely handicapped ¥300,000
- (vii) Exemption for a widow, widower, or working student
- If a taxpayer is a widow, widower, or working student
..... ¥260,000
- However, ¥300,000 is the deduction for widows whose total income is below ¥5 million and who are raising a child (children) as a dependent (dependents).
- (viii) Exemption for spouses
- An deduction of ¥ 330,000 (¥380,000 for those who are 70 years old or older) is allowed for a spouse whose income for the previous fiscal year was ¥380,000 or less. In a case whose the spouse subject to tax deduction is especially handicapped and is sharing the same house with the taxpayer, a deduction of ¥560,000 (¥610,000 for such spouse who

is 70 years old or older) is allowed.

(ix) Special Exemption for spouses

An exemption is allowed for a spouse who is not subject to tax deduction and lives with a taxpayer whose amount taxable income is no more than ¥10 million. The amount of deduction varies according to the spouse's income. The maximum amount is ¥330,000.

(x) Exemption for dependents ¥330,000

This exemption applies only to taxpayers whose dependent's income is no more than ¥380,000.

For elderly dependents (70 years or older, excluding the spouse)

..... ¥380,000

For dependents who are from 16 to 22 years old ¥450,000

In case the lineal ancestor who is sharing the same house with a taxpayer or his order spouse is an aged dependant. ¥450,000

In case a dependent sharing the same house with the taxpayer is especially handicapped, ¥230,000 shall be added to the above amount of deduction.

(xi) Basic Exemption ¥330,000

(xii) When income is less than $¥350,000 \times (1 + \text{number of dependents including spouse}) + ¥320,000$ (when a taxpayer has a spouse or dependents), such a person is not taxable.

(xiii) Standard Tax Rates

The standard tax rates mentioned below apply to taxable income.

Taxable Income		Tax Rate
Over	But not over	
—	¥2,000,000	3 %
¥2,000,000	¥7,000,000	8 %
¥7,000,000		10 %

Note) Standard tax rate is uniformly 6% after FY2007 along with the transfer of tax revenue from the National income tax to the Local inhabitants tax.

The following tax credits are allowed not only with respect to the municipal inhabitants tax but also the prefectural inhabitants tax, excluding those assessed on a 'per capita' basis.

Credit	Prefectural Inhabitants Tax	Municipal Inhabitants Tax
Credit for dividends	0.8%(1.2%) of dividend income (If taxable income, including dividends, exceeds ¥10 mil-	2%(1.6%) of dividend income (If taxable income, including dividends, exceeds ¥10 million, 1%

XXIII Local Taxes

	lion, 0.4%(0.6%) of the dividend income corresponding to the excess amount) (see 2/5,5.a)	(0.8%) of the dividend income corresponding to the excess amount) (see 2/5,5.a)
Credit for foreign taxes	When a taxpayer of the part of inhabitants tax which is proportional to his/her income is assigned foreign income tax or tax which corresponds to the part of prefectural inhabitants tax which is proportional to his/her income and interest income, and proportional part of municipal inhabitants tax (We call them “foreign income tax etc.”), and the amount foreign tax etc. exceeds the limit of tax credit which is stipulated in the Income Tax Law, a taxpayer can deduct these excessive amount from the part of tax which is proportional to his /her income to 10% (12%) of the limit of tax credit of income tax .	If a taxpayer has the amount of foreign tax etc. which cannot be deducted from income tax and prefectural inhabitants tax, a taxpayer can deduct these amount from the part of tax which is proportional to his /her income to 20% (18%) of the limit of tax credit of income tax .

Note) The figures in parenthesis are tax rates applied for local inhabitants tax after FY2007.

- (b) Special tax treatment of capital gains derived from the transfer of land, buildings, or rights to use land

Both prefectural and municipal inhabitants taxes are levied on capital gains derived from the sale or transfer of land, buildings and rights to use land, separately from these other incomes.

Tax rates applicable to such capital gains are as follows:

Note) The figures in parenthesis are tax rates applied for local inhabitants tax after FY2007.

- (i) Long-Term Capital Gains

Capital gains derived from continuously owned for more than 5 years as of 1 January of the year in which the transfer was made are classified as long-term capital gains.

- ① General provisions

Rates vary according to the amount of taxable capital gains. Taxable capital gains are obtained by subtracting the amount of statutory deductions. Increased deductions varying from ¥8 million

to ¥50 million are available according to the type of transfer and assets.

Prefectural Tax	Municipal Tax
1.6%(2.0%) of T.L.C.G.	3.4%(3.0%) of T.L.C.G.

[Notes] T.L.C.G.: Taxable Long-Term Capital Gains

- ② Special provisions for land or rights to use land transferred to the State, etc.

In the case of transfer of land or rights to use land to the State, local governments, or other specified public entities, or to persons engaging in the preparation of large-scale and desirable housing sites, T.L.C.G. is taxed at reduced rates. Rates vary according to the amount of capital gains.

	Prefectural Tax	Municipal Tax
¥20 million or less	1.3%(1.6%) of T.L.C.G.	2.7%(2.4%) of T.L.C.G.
exceeding ¥20 million	T.L.C.G. × 1.6%(2.0%) + ¥260,000	T.L.C.G. × 3.4%(3.0%) + ¥540,000

[Note] T.L.C.G.: Taxable Long-Term Capital Gains

- ③ Capital gains deriving from the transfer of residential property co-tenuously owned for over 10 years as of 1 January of the year in which the sale was made.

Rates vary according to the amount of taxable capital gains.

	Prefectural Tax	Municipal Tax
¥60 million or less	1.3%(1.6%) of T.L.C.G.	2.7%(2.4%) of T.L.C.G.
exceeding ¥60 million	(T.L.C.G. - ¥60 million) × 1.6%(2.0%) + ¥780,000	(T.L.C.G. - ¥60 million) × 3.4%(3.0%) + ¥1,620,000

[Note] T.L.C.G.: Taxable Long-Term Capital Gains

- (ii) Short-Term Capital Gains

Capital Gains deriving from the transfer of property owned for no more than 5 years as of 1 January of the year in which the transfer was made are classified as short-term capital gains.

Prefectural Tax	Municipal Tax
3.0%(3.6%) of T.S.C.G.	6.0%(3.4%) of T.S.C.G.

[Note] T.S.C.G.: Taxable Short-Term Capital Gains

In the case of transfer to the state, local government, etc..

Prefectural Tax	Municipal Tax
1.6%(2.0%) of T.S.C.G.	3.4%(3.0%) of T.S.C.G.

[Note] T.S.C.G.: Taxable Short-Term Capital Gains

(c) Special Tax Treatment of Capital Gains Derived from the Transfer of Securities

Capital gains derived from the sale or transfer of the flowing securities is taxed separately from other incomes.

- (i) Stocks (including the right to accept stocks or accept/subscribe new stocks)
- (ii) Shares of investors in a limited partnership, an unlimited partnership, and a limited company
- (iii) Bonds with rights to subscribe to new stocks
- (iv) Preferential investment
- (v) Beneficiary certificates of investment trusts on securities such as stocks
- (vi) Beneficiary certificate of certain special purposes trusts

Capital gains derived from the sale or transfer of the securities mentioned above are taxed separately when filing a return. The tax rate applicable to the above capital gains are 1.6%(2.0%) for prefectural tax and 3.4%(3.0%) for municipal tax. The tax rates for capital gains from the sale of listed stocks during the period from 2004 to 2008 are 1%(1.2%) for prefectural tax and 2%(1.8%) for municipal tax.

Out of the amount of losses arising from transfer of listed stocks, etc. from January 1, 2003 onward, those that are not deductible during the relevant year may be carried forward to be deducted within three years thereafter from the capital gains, etc. derived from the transfer of stocks.

Note) The figures in parenthesis are tax rates applied for local inhabitants tax after FY2007.

The following exceptions are allowed:

- (i) In a case where listed stocks, etc. acquired before September 30, 2001 are to be transferred during the period from January 1, 2003 to December 31, 2010, the acquisition cost may be regarded by option to be 80% of the price as of October 1, 2001.
- (ii) In a case where listed stocks, etc. purchased by an individual person during the period from November 30, 2001 to December 31, 2002 are transferred from 2005 to 2007, the capital gain derived from such a transfer is not taxed if the purchase price was less than ¥10 million. (“Urgent investment incentive measure”)

The tax on the residents of prefectures for capital gains from each

sale of stocks

With regard to the tax on incomes from transfers of stocks within an account for withholding tax (i.e. the special account for withholding tax at source) earned during the period from January 1, 2004 onward, the securities company to pay such incomes shall make special collection and pay the taxes to the prefecture concerned.

The tax rate is 5% (but 3% for the incomes paid during the period from January 1, 2004 to December 31, 2007).

The prefecture concerned shall deliver the amount equivalent to 2/3 of the income levy on capital gains from transfer of stocks (3/5 for the amount allocated after August 2007) to cities, towns and villages.

- (d) Special exception for dividend incomes from stock dividends, etc.

Prefectural inhabitants tax on dividend basis

With regard to the tax on incomes from special dividends, etc., on shares during the period from January 1, 2004, onward, the securities company to pay such incomes is to make a special collection and pay the taxes to the prefecture concerned.

The tax rate is 5% (but 3% for the incomes paid during the period from January 1, 2004, to March 31, 2008).

The prefecture concerned shall deliver the amount equivalent to 2/3 of the income levy on dividends (3/5 for the amount allocated after August 2007) to cities, towns and villages.

* Special dividends, etc.: dividends from certain listed stocks, dividends from publicly-offered securities investment trusts other than publicly-offered bond investment trusts, dividends from publicly-offered foreign securities investment trusts other than publicly-offered foreign bond investment trusts, dividends of profit from investments of special investment firms, etc.

- (e) Special cases for miscellaneous incomes from transactions of futures

In case futures are transacted and the balance of such transactions is settled, tax shall be imposed on the income at the rates of 1.6%(2.0%) for prefectural tax and 3.4%(3.0%) for municipal tax separately from other incomes.

Note) The figures in parenthesis are tax rates applied for local inhabitants tax after FY2007.

Out of the losses arising from transactions of futures made during the period from January 1, 2003 onward and once the balance is settled, the loss remaining after deduction is made in the relevant year may be subject to a deferred deduction over three years beginning with the year following

XXIII Local Taxes

the year of the transaction from the miscellaneous incomes obtained from transactions of futures.

(2) Corporations (income rate)

Taxable income is basically the amount of national Corporation tax. The standard tax rate for corporations is 12.3%. The rate should not exceed 14.7%.

(3) Per capita tax rates

The rates for per capita tax are as follows:

(a) Individuals

¥3,000 (Standard rate)

(b) Corporations

Capital plus Reserve Fund	Employees	Standard	Maximum
More than ¥5 billion	More than 50	¥3,000,000	¥3,600,000
	50 or less	¥410,000	¥492,000
More than ¥1 billion but not more than ¥5 billion	More than 50	¥1,750,000	¥2,100,000
	50 or less	¥410,000	¥492,000
More than ¥100 million but not more than ¥1 billion	More than 50	¥400,000	¥480,000
	50 or less	¥160,000	¥192,000
More than ¥10 million but not more than ¥100 million	More than 50	¥150,000	¥180,000
	50 or less	¥130,000	¥156,000
Not more than ¥10 million	More than 50	¥120,000	¥144,000
	50 or less	¥50,000	¥60,000

[Note] Maximum rates are obtained by multiplying the standard rates by 1.2. Municipalities can raise their rates. (see 23/4, b.(2)) For individuals, there are no maximum rates.

c. Payment

Inhabitants tax is collected by self-assessment unless it is withheld at the source. Under the self-assessment system, individual taxpayers are required to file a return for their annual income in the previous year not later than 15 March. However, when individual taxpayers file returns regarding national income tax, they are deemed to file returns regarding municipal inhabitant tax. Payments are usually made in four installments June, August, October, and January of the following year. Wage earners usually pay the tax under the special collection system, in which the employer deducts the tax from monthly wages over a 12-month period from June to May and pays the amount monthly. When there are wage earners with low income in a municipality, however, the ordinary correction system may be adopted in place of the special collection system.

In the case of a corporation, declaration and payment are generally made within two months of the close of the accounting period. If a corporation has offices or places of business in two or more cities, towns, or villages, the tax amount paid is determined by prorating the total tax on the basis of the number of employees in each office.

2. Property Tax

a. Taxpayers

Persons listed as owners of fixed assets in the tax cadastre as of 1 January each year must pay property tax to the municipality where the property is located for the fiscal year beginning in April of that year. The obligation for payment remains even if ownership is transferred during the year.

b. Tax Base

Taxable assets for property tax purposes are, Land, Houses, Depreciable assets.

Automobiles and light vehicles are exempt from property taxes purposes, as they are already subject to the automobile tax (23/3, 7) and light vehicle tax (23/4, 3).

The tax base for property tax is, in principle, the price of land, houses and depreciable assets and those registered on the tax cadastre. With respect to land, complex measures to adjust burdens are established. The cadastral value is revised every three years according to a survey of market prices for land and houses. From the view point of housing policy, the tax base for houses and housing land shall be reduced as follows.

Land for housing: One-sixth for a portion up to 200 square meters and one-third for a portion exceeding 200 square meters.

New houses: certain residential houses built in the period from January 2, 1963 to March 31, 2008 with floor space between 50 m² and 280 m²: one-half for the first three years only.

Certain new fire-proof residential buildings with three or more stories built during the period from January 2, 1964 to March 31, 2008, for which the floor space is between 50 m² and 280 m² : one-half for the first five years only.

c. Tax Rate

The standard tax rate is 1.4%.

d. Exemptions

The tax is not applied in principle where the tax base of assets owned by a

XXIII Local Taxes

taxpayer is below the threshold listed.

Land ¥300,000

Housing ¥200,000

Depreciable assets ¥1,500,000

Fixed assets owned by organizations working for public benefit and used for public benefit are exempt from property tax.

Fixed assets used for certain purposes such as cemeteries and public roads are also exempt.

e. Payment

Property tax is generally paid in 4 installments: April, July, December, and February of the following year. The tax cadastre for fixed assets is made public for 20 days or longer from 1 April every year.

3. Light Vehicle Tax

a. Taxpayers

Owners of light vehicles or other small vehicles.

b. Tax Base and Tax Rates

The objects of taxation are motorbikes, motorcycles, and two, three, and four-wheeled light vehicles used for transportation.

Standard annual tax rate is calculated according to the type of vehicle as follows:

1. Motorbikes

- (1) Motorbikes with a cylinder volume not over 50 cc or with related power not over 0.6kW (excluding the motorbikes mentioned in (4)) ¥1,000
- (2) Motorbikes with two wheels with a cylinder volume 50–90 cc or with related power 0.6–0.8kW ¥1,200
- (3) Motorbikes with two wheels with a cylinder volume over 90 cc or with related power over 0.8kW ¥1,600
- (4) Motorbikes with three or more wheels with a cylinder volume over 20 cc or with related power over 0.25kW ¥2,500

2. Light vehicles and small special vehicles

- (1) with two wheels (including ones with sidecars) ¥2,400
- (2) with three wheels ¥3,100
- (3) with four or more wheels
for passenger
for commercial use ¥5,500

for non-commercial use	¥7,200
for freight	
for commercial use	¥3,000
for non-commercial use	¥4,000
3. Small vehicles with two wheels (motorcycles).....	¥4,000

c. Payment

Payment is due in April.

4. Tobacco Tax

The tax basis is the same as the prefectural tobacco tax (see 23/3, 5).

5. Mineral Product Tax

a. Taxpayers

Persons engaged in mining.

b. Tax Base and Tax Rates

The standard tax rate and the ceiling rate are 1% and 1.2%, respectively, of the value of the mineral products mined.

In the case of mines with a monthly production under ¥2 million, the reduced standard rate of 0.7% applies, the maximum rate being 0.9%. Methods of payment are determined by local ordinance and the day of payment is between 10th and the end of every month.

6. Special Landholding Tax

A special landholding tax was introduced in 1973 as part of a series of reforms in land taxation designed to thwart speculation. However, taxation is suspended from FY 2003 for the time being.

The tax consists of two measures:

(1) Special tax on the holding of land

The taxable object is land held. Land is excluded from the tax when it has been held for over ten years.

(2) Special tax on land acquisition

The taxable object is land acquired.

a. Taxpayers

Landowners or persons who acquire land.

b. Tax Base and Tax Rates

- (1) Special landholding tax on holding of land

The tax amount is 1.4% of the acquisition cost of land held on January every year. The amount corresponding to property tax calculated at the standard rate (1.4%) on the land concerned may be credited for payment of this tax.

- (2) Special landholding tax on land acquisition

The amount of tax is 3% of the acquisition cost of land acquired within one year before 1 January or 1 July. The amount corresponding to Real property acquisition tax is credited for payment of this tax.

c. Exemptions

When the land area concerned is smaller than the prescribed area, which varies in 2,000 m², 5,000 m² or 10,000 m², depending on the municipality, the tax is not applied.

d. Non-taxable Cases

The following land is not subject to this tax:

Land subject to the state, etc.

Land acquired by corporate merger or inheritance and;

Land used for specific state or local public policy, such as expansion of agricultural operations, forestry, or decentralization of factories.

e. Taxation on Idle Land

- (1) As for land with an area of more than 1,000 m² within an area designated in city planning as a “District for Identifying and Promoting the Utilization of Idle Land,” Special Landholding Tax is levied on the tax base of the current price or the acquisition cost, whichever is higher.

- (2) Tax rate: 1.4% (Property Tax and ordinary Special Landholding Tax is credited to this tax liability.)

f. Payment

The tax must be paid on a self-assessment basis by the following dates:

- (1) For the special landholding tax on the holding of land, the end of May in the year concerned.
- (2) For the special landholding tax on the acquisition of land, the end of February or August in the year concerned.

7. Bathing Tax

Revenue from this tax is used for the improvement of tourist facilities.

a. Taxpayers and Tax Amount

A person who bathes in a hot-spring is subject to the tax. The standard tax amount is ¥150 per day, per person.

b. Payment

The tax is specially collected at hot-spring hotels, etc. Details of payment are determined by local ordinance.

8. Urban Planning Tax

Cities, towns, and villages undertaking projects under the Urban Planning Law may levy this tax on owners of land and buildings located within urbanization areas. The appraised value is used as the basis of assessment for the property tax.

The ceiling tax rate is 0.3% and is collected together with property tax.

9. Business Office Tax

Business Office Tax, which was introduced in the 1975 tax reform, is levied on business activities in a building. Revenue from this tax is used for the improvement of urban environments.

a. Taxing Entities

Local public entities that can levy the business office tax are limited as follows:

- (1) Tokyo (23 special wards) and the fifteen largest cities (Sapporo, Sendai, Chiba, Saitama, Kawasaki, Yokohama, Shizuoka, Nagoya, Kyoto, Osaka, Sakai, Kobe, Hiroshima, Kitakyushu, and Fukuoka)
- (2) The Cities of Musashino, Mitaka, Kawaguchi, Moriguchi, Higashi-Osaka, Amagasaki, Nishinomiya, and Ashiya
- (3) Cities with a population no less than 300,000, to be designated by cabinet order.

b. Tax Base and Tax Rates

- (1) Tax on business activity in a building

The tax amount is ¥600/m² of the building's floor space and 0.25% of the total remuneration paid to employees.

c. Taxpayers

Person(s) conducting business in that building

d. Tax Exemption

Business office tax is exempted in the following cases:

- (1) Tax on assets: businesses with a building floor space of no more than 1,000 m²;
- (2) Tax on employees: businesses with no more than 100 employees.

e. Payment

Business office tax is collected by self-assessment and must be paid when filing a return.

- (1) Individual taxpayers are required to file a return no later than 15 March
- (2) Corporate taxpayers are required to file a return within two months of the close of an accounting period.

10. Other Taxes

- (1) General and Object tax not stipulated in Local Tax law

Thirteen municipalities levy taxes items other than those approved by the Minister of Internal Affairs and Communications and specified in the Local Tax Law subject to the approval of the Minister of Internal Affairs and Communications. For example, the City of Atami levies Tax for the Possession of Resort Villas.

- (2) Other Taxes

Other tax items established by cities, towns and villages are Water and Land Utilization Tax, Public Facilities Tax, Land Development Tax and National Health Insurance Tax.

CHAPTER XXIV

TAXATION OF NONRESIDENTS AND FOREIGN CORPORATIONS

24/1 Taxation of Nonresidents

1. Classification of Taxpayers and Their Tax Liabilities

- a. Individual taxpayers are classified into the following categories:
 - (1) Resident*—an individual with a domicile or residence in Japan for a period of one year or longer.
 - (2) Nonresident—an individual other than a resident.
- b. A resident taxpayer is subject to income tax on worldwide income, while a nonresident taxpayer is subject to income tax solely upon income from sources within Japan.
- c. A resident taxpayer, who does not have Japanese nationality and has lived in Japan for not more than five years in the past ten years, is deemed as “a non-permanent resident”. A non-permanent resident taxpayer is subject to income tax solely on ① income derived from sources within Japan and ② income derived from foreign sources paid in Japan or remitted to Japan.

2. Income from Sources within Japan

a. General Description

The following items are treated as income from sources within Japan (The Income Tax Law § 161), unless otherwise stipulated in tax treaties for the avoidance of double taxation:

- (1) Income from business conducted in Japan or from the use, holding, or sale of an asset situated in Japan (excluding the income items specified in (2) to (14) below) and other income from sources within Japan**.

* (1) An individual who has come to Japan is presumed immediately upon his arrival to be a resident of Japan if:

- (a) Such an individual has an occupation, vocation, profession, or contract of employment which, under normal conditions, requires continuous residence in Japan for a period of one year or longer or;
- (b) Such an individual possesses Japanese nationality or the immigration status of a permanent resident of Japan and any factors, such as the residence of a spouse and children in Japan, that warrant the supposition that he or she will stay in Japan for a period of one year or longer.
- (2) A national or local government official serving abroad is deemed to have a domicile in Japan as long as he or she is a Japanese national.

** The following items are treated as income from sources within Japan:

- (1) Insurance or indemnity obtained with respect to business carried out in Japan or of assets situated in Japan

- (2) Dividend from the union business in Japan.
- (3) Income from the transfer of lands and buildings situated in Japan.
- (4) Income from business that consists primarily of providing personal services* performed in Japan.
- (5) Rent or other compensation for the use of immovable property, including rights thereon, located in Japan. Royalties for the use of quarrying rights or mining rights granted under Japanese law and rental from a bareboat charter of a ship or aircraft for which the lessee is a Japanese resident or a domestic corporation.
- (6) Interests, which is yielded on national and local government bonds, bonds issued by domestic corporations, and deposits left in offices residing in Japan, and distribution of profits from joint operation trusts and bond trusts, which is entrusted with offices residing in Japan
- (7) Dividends and distributions of surpluses and profits from domestic corporations, and distribution of profits from security investment trusts, which is entrusted with offices residing in Japan. (excluding bond investment trusts)
- (8) Interest on loans**, when the money lent is used for business conducted in Japan by the debtor.
- (9) Royalties (not depending on whether it is temporary or continuous) for the use of, or the right to use, patents (including know-how), copyrights (including the rights to use motion picture films, television films, or video-tapes), their neighboring rights, or equipment and proceeds from the sale of patents or copyrights, when such royalties or considerations are paid for those properties by a person conducting business in Japan.
- (10) Salaries, wages, or other remuneration, including pensions or retirement allowances, except for foreign pensions or retirement allowances.
- (11) Awards or similar profits for advertisements provided in Japan.

(2) Donations of assets situated in Japan, excluding donations from individuals

(3) Income from buried properties or lost properties discovered in Japan

(4) Awards from prize-contests held in Japan

(5) Windfall profits other than those included in (2) to (4) above, realized in consequence of an act performed in Japan

(6) Profits other than those specified in (1) to (5) above (such as the profits derived from a waiver of obligation) obtained with respect to business conducted in Japan or of assets situated in Japan

* “Personal services” in this context consist of the following types of services:

(1) Public entertainers or athletes

(2) Professional services, such as those of lawyers, accountants, or architects

(3) Scientific, technical, or managerial expertise or skill (excluding those services incidental to the main business activities of the enterprise concerned, such as the sale of machinery or equipment and personal services for the supervision or superintendence of construction, installation, or assembly activities)

** Not including interest or similar payments on shippers’ usance bills and banks’ import usance bills, the term of which is no more than six months

- (12) Annuities (other than those falling under the category of (10) above) on life insurance, indemnity insurance, or similar contracts concluded through a place of business in Japan.
- (13) Interests, profits, or premiums accrued from quasi-financial products such as foreign currency time deposits, gold deposit accounts, mortgage backed securities, etc.
- (14) Distribution of profits under a sleeping partnership contract or similar contract for the purpose of investment in business conducted in Japan.

b. Income from Business Conducted in Japan ((1) income in a. above)

In allocating profits from a business conducted concurrently Japan and abroad, the allocation of income between Japanese and foreign sources is determined according to the following criteria:

- (1) For the sale of goods or merchandise in Japan that are acquired outside Japan and are not processed outside Japan, the total income from such sale is deemed to arise in Japan*;
- (2) For the sale of goods or merchandise in and outside Japan, income from such sale is allocated among the countries concerned on the basis of normal transactions at arm's length;
- (3) For construction, installation, or assembly projects undertaken in Japan, the total income derived from such activities is treated as arising in Japan, even if the contract thereof is concluded or the labor or materials are procured outside Japan;
- (4) For international maritime transportation, income is allocated to Japanese sources based on the ratio of revenue from outgoing passengers and cargoes from Japan to worldwide revenue; in the case of international air transportation, the allocation will be made on the basis of revenue obtained, expenses incurred in connection with work executed in Japan, the value of assets situated in Japan, or other reasonable factors;
- (5) For insurance businesses, income derived from contracts concluded through a place of business or an agent located in Japan is treated as arising in Japan;
- (6) For advertising activities carried on by publishing or broadcasting enterprises, for or on behalf of others, income derived is treated as arising in Japan, to the extent that such advertising is used in Japan;

* The sale or disposal of goods or merchandise is deemed to be made in Japan, if:

- (1) Such goods or merchandise are actually in Japan or are under the control of the permanent establishment of a seller situated in Japan immediately before delivery
- (2) The contract for the sale or disposal is concluded in Japan, or
- (3) A substantial part of the negotiation for the sale or disposal is conducted in Japan

- (7) In cases other than those mentioned in (1) to (6) above, the scope of income from sources in Japan is determined on the basis of normal transactions at arm's length, or of a reasonable apportionment of worldwide business income according to factors such as revenue obtained or expenses incurred, in connection with occupations performed in Japan, or the value of assets situated in Japan, etc.

In applying the above criteria, no income will be deemed to arise from, or in connection with, the following activities*:

- (a) Activities auxiliary to the main business of an enterprise, such as advertising, publicity, collection of information, basic research, etc., as long as such activities are conducted by one section of an enterprise on behalf of another section of the same enterprise, regardless of the location of the sections involved or;
- (b) Intra-company transfer or use of money, patents, or other assets between departments or branches of a foreign enterprise.

Notwithstanding the above criteria (1) through (7), income accrued from overseas investment through a branch of a foreign enterprise located in Japan is treated as income from business conducted within Japan, unless such income is taxable in a foreign jurisdiction, other than a country in which the headquarters of the foreign enterprise is situated, where such investment was made.

c. Income from the Use, Holding, Sale, or Disposal of an Asset Situated in Japan ((1) income in a. above)

- (1) Income from the utilization or holding of an asset situated in Japan includes:
 - (a) Redemption premiums (the difference between the redemption price and the issuing price) obtained from national or local government bonds or debentures issued by domestic corporations or commercial papers issued by domestic corporations and;
 - (b) Interest on loans provided to a resident or individuals other than those related to the debtor's business (covered by item 2. a. (8))
- (2) Income from the sale or disposal of assets includes:

* As a corollary, the rules for the calculation of income from business conducted in Japan can be set forth as follows:

- (1) No profit will be attributed to a branch of an enterprise situated abroad with respect to auxiliary activities performed abroad for the same enterprise situated in Japan and,
- (2) Charges for the use of funds, patents, or other assets supplied to a Japanese branch of an enterprise from the head office or foreign branches of the same enterprise are deductible as expenses only to the extent of costs incurred by the head office or foreign branches to supply such assets.

- (a) Sale or disposal of rights or licenses granted under the provisions of Japanese law;
- (b) Sale of securities when the sale is made in the market of the Stock Exchange or through a place of business of the dealer or broker (including a branch of the foreign dealer or broker) located in Japan;
- (c) Sale of forestalled shares of a domestic corporation;
- (d) Sale of a substantial interest in a domestic corporation, i.e., the sale, made by a nonresident, his relatives or subordinate companies, of 5% or more of the issued shares of a domestic corporation within the year of sale, if they have owned 25% or more of such issued shares during the year of sale, or during the preceding two years and;
- (e) Capital gains from the transfer of stocks of real estate corporation or equities of special trust funds related to real estate.
- (f) Sale or disposal of the rights of business conducted in Japan.

3. Classification of Nonresident Taxpayers and Respective Taxable Income

a. Nonresidents are classified for income tax purposes into the following four categories depending on their type of permanent establishment (PE) and so on:

- (1) A nonresident who has a branch, sub-branch, office, factory, mine, quarry, or other fixed place of business* in Japan (“subparagraph (1) PE”).
- (2) A nonresident, other than that of type (1) above, who undertakes construction, installation, or assembly activities or provides personal services for the supervision or superintendence of such activities for more than one year in Japan (“subparagraph (2) PE”).
- (3) A nonresident, other than that of type above, who carries out business in Japan through the following agents (“subparagraph (3) PE”):
 - (a) A person having and habitually exercising the authority to conclude contracts in Japan for, or on behalf of, the nonresident**, unless the activities of such a person are limited exclusively to purchasing goods or merchandise;
 - (b) A person habitually maintaining in Japan a stock of goods or merchandise from which he or she fills orders and makes deliveries on behalf of the nonresident; and

* “Fixed place of business” in this respect does not include the use of facilities solely for the storage of goods or merchandise belonging to the nonresident, nor a place of business used solely for the purchasing of goods or merchandise, or for advertising, publicity, scientific research, or similar activities of an auxiliary character for the nonresident.

** However, a person who engages in the same kind of business as that of the nonresident and exercises authority to conclude contracts for the latter because the very nature of such (international) business is not considered for an agent of this category.

- (c) A person habitually securing orders, negotiating, or performing other important activities in Japan to conclude contracts, exclusively or almost exclusively, for or on behalf of the nonresident.
- (4) A nonresident other than any of (1) to (3) above (a nonresident without PE).

b.(1) Tax treatment differs according to the type of nonresident.

- (a) The nonresident mentioned in a (1) above is subject to “aggregate income taxation,” i.e., taxation at the normal graduated tax rates, based on his or her net income (see 2/5, 1), from his or her entire Japanese source income.
- (b) A nonresident falling under category (2) or (3) above is subject to “aggregate income taxation” on total income from (1) to (5) in 2. a above, and on such parts of his or her income from (7) to (12) and (14) in 2. a above, as is attributable to business conducted through a permanent establishment in Japan. Such parts of his or her income from (5) to (10) and (12) in 2. a that are not attributable to business conducted through a permanent establishment are subject only to withholding “separate income taxation” at the flat rate of 20% of gross revenue.
- (c) In the case of the nonresident mentioned in (4) above, the “aggregate income taxation” is applied only to parts of income in (1) and (3)* in 2. a above and total income in (4) and (5) in 2. a above, while income of from (7) to (12) and (14) in 2. a of such a nonresident is always subject to only 20% withholding “separate income taxation.”
- (2) (1) above notwithstanding, income belonging to categories (6) and (13) in 2. a above are subject to 15%, and income from securities investment trusts and certain listed stocks that are included in income category (7) are subject only to “Withholding taxation” at the rate of 7% of gross income. This format tax treatment is common to all types of nonresidents in 3. a.
- (3) (1) above notwithstanding, with respect to Japanese-source income derived by all types of nonresidents from the disposal of stocks, convertible bonds etc., which are included in category (1) in 2. a above, the net capital

* The part of income in (1) in 2. a. that is taxable for the nonresident without PE mentioned in (4) consists of income from the following items as well as occasional income arising in Japan:

- (1) Utilization or holding of assets situated in Japan
- (2) Sale or disposal of immovable properties (including rights thereon) located in Japan
- (3) Disposal or cutting of timber standing in Japan
- (4) Sale of forestalled shares (including shares designated by the Stock Exchange as “special information issues”) or of substantial participation in a domestic corporation
- (5) Capital gains from the transfer of stocks of real estate corporation or equities of special trust funds related to real estate.
- (6) Disposition of assets in Japan other than those mentioned in (1) to (5) while staying in Japan.

gain will be taxed separately at the rate of 15% through the filing of tax returns. However, as for the transfer of listed stocks and other publicly traded securities of investment trusts, if the nonresident has any PE in Japan, he or she is imposed on the rate of 7% tax and can elect to be taxed under “withholding taxation” by submitting certain forms via a security company.

4. Principle of Tax Calculation

- a. The method for calculating taxable income and tax thereon for the purpose of “aggregate income taxation” of a nonresident taxpayer is generally the same as that for a resident taxpayer. That is to say, provisions in the laws and cabinet orders for the calculation of a tax base and the amount of income tax (see 2/3—2/5) applicable to a resident are likewise applied, *mutatis mutandis*, to a nonresident subject to “aggregate income taxation.”

An exception to this principle is, however, that deductions, exemptions, or tax credits are not allowed for nonresident taxpayers, except for deductions for casualty losses and contributions, basic exemptions, and credit for dividends (see 2/4 and 2/5, 4. (a)). Casualty losses are recognized only on the assets owned by a nonresident taxpayer that are situated in Japan.

- b. A flat rate of 20%* is applied to the gross revenue of the income items subject to “separate income taxation.” In these cases, income tax withheld at the source with respect to such income items becomes the final tax liability of the recipient. If a tax convention is in existence, special reduced rates or exemptions might be applied (see 24/3).

5. Special Taxation Measures Applicable to a Nonresident Taxpayer

The Special Taxation Measures Law also provides the following forms of treatment for nonresident taxpayers:

- (1) The following items are not subject to income tax if ① they are derived by a nonresident with no permanent establishment in Japan or ② they are derived by a nonresident who has a permanent establishment, but they are not attributable to the permanent establishment through which his or her business is conducted in Japan:
 - (a) The part that corresponds to the holding period of the taxpayer of the

* In the case of retirement income, however, a nonresident has a choice of paying either:

- (1) 20% of the gross amount of retirement income from sources in Japan or;
- (2) an amount computed in the same way as a resident is taxed on his retirement income on the basis of the entire retirement income (including such income from sources abroad). And tax rate imposed on income of 3.b(2)(3) is 15% or 7%.

interest from transferable government bonds paid to nonresidents who meet certain conditions.

(b) Interest or redemption premiums (the excess of the redemption price over issuing price) on bonds or debentures issued abroad by domestic corporations.

(2) Redemption premiums of certain discount bonds are subject to withholding “separate income taxation” at the rate of 18% (or 16%)*.

6. Withholding Income Tax at the Source

- a. Anyone who pays income classified under items 2.a (2) to (14) in Japan to a nonresident is required to withhold income tax** at the rate of 20% (7%, 10% or 15% for certain categories of income (see 3.b)) and to pay the tax thus withheld to the government before the 10th day of the month following the month of withholding. If payment to a nonresident or foreign corporation is made abroad (e.g., through a paying agent located abroad), the payer must withhold and pay the tax if the original payer is a resident, a domestic corporation, a nonresident having temporary residence, a permanent establishment in Japan, or a foreign corporation having a permanent establishment in Japan. In the latter case, payment of tax to the government must be made before the end of the month following the month of payment.
- b. If the recipient is a nonresident having a permanent establishment in Japan, withholding tax may be exempted for the following types of income, provided that the recipient obtains from the Tax Office a certificate*** stating that such income is subject to tax together with his or her other income from business in Japan, and presents it to the payer of income:
 - (1) Income classified under items (2), (4), (5), (8), (9), reward for service in (10) and (12) in 3.a that is received by a nonresident of type (1) in 3.a above.
 - (2) Income mentioned in (1) above that is received by a nonresident of type (2) or (3) in 3.a above and is attributable to his or her business is conducted at a permanent establishment in Japan.
- c. For income (2.a (4)) from businesses that consist of providing personal services by nonresident or foreign corporation, if a withholding has been made,

* If the maximum tax rate on redemption premiums is reduced by the double taxation convention, a reduction tax rate is applicable.

** In case the income related to (2.a,(2)) is not paid by the day when two months pass from the next day of the last day of a calculation period stipulated in a contract of partnership, the payment is considered to be made on the day and the payer must withhold taxes.

*** Such a certificate is given on request to a nonresident stating that the income item concerned is subject to “aggregate income taxation” and that he or she had filed an income tax return for the previous year.

the nonresident operator of such business is not required to withhold income tax when he or she pays, out of such receipts, salaries or other remunerations (2.a (10)) to individual nonresidents actually performing such personal services.

7. Special Rules for Filing a Return and Paying Tax

- a.** A nonresident liable for “aggregate income taxation” must pay tax by filing a final return (see 2/6 and 2/7). The following nonresidents are also required to file a final return and pay the tax thereon at the times mentioned respectively:
- (1) A nonresident having temporary residence in Japan—at the time of leaving Japan if he or she does not appoint a tax agent in Japan and report such to tax authorities.
 - (2) A nonresident having no temporary residence but having a permanent establishment in Japan—at the time of closure of the permanent establishment.
 - (3) A nonresident having neither temporary residence nor permanent establishment in Japan but operating a business (2.a (4)) that consists primarily of providing personal services in Japan—at the time of terminating such operations in Japan.

If (1), (2), or (3) occurs during the period from 1 January to 15 March, a nonresident falling under this category must file a final return for the previous year as well as a final return for the current year.

- b.** A nonresident liable only for “separate income taxation” is required to file a quasi-final return and pay the tax due thereon if withholding tax has not been imposed with respect to salaries or remuneration (2.a (10)) from sources within Japan. The final date for filing such a return is 15 March of the following year, or the date of departure from Japan, whichever is earlier. If a nonresident liable only for the “separate income taxation” has elected the option described in the footnote to 4.b above he or she may file a return after the day, when he or she can receive the entire amount of retirement allowance, or January 1 after the taxes on retirement income were withheld, and claim a refund, if any, of an amount equal to the difference in the tax due on the return and the tax withheld.

8. Jurisdiction over Taxation Matters for Nonresidents

The Tax Office having jurisdiction over taxation matters for a nonresident is determined on the basis, of, in order, the following:

- (1) Place of residence in Japan

- (2) Place of permanent establishment in Japan
- (3) Place of residence of relatives living continuously in Japan after his or her departure
- (4) Location of immovable properties in Japan from which income for item (5) in 2. a above (excluding rental from a bare boat or full charter) accrues
- (5) Place which has hitherto been determined under (1) to (4) above
- (6) Place that he or she has selected for filing returns, making claims, etc.
- (7) Place under the jurisdiction of the Kojimachi Tax Office, in Tokyo

24/2 Taxation of Foreign Corporations

1. Tax Liabilities-General Rule

A foreign corporation is subject to corporation tax and/or income tax upon its income from sources within Japan.*

2. Income from Sources within Japan

- a. The following items are treated as income from sources within Japan unless otherwise stipulated in tax treaties for the avoidance of double taxation Article (refer also to 24/1, 2):
 - (1) Income from business conducted in Japan or from the utilization, holding, sale, or disposal of assets situated in Japan and other income sources within Japan (excluding the income items specified in (2) to (11) below).
 - (2) Income from businesses that consist primarily of providing personal services performed in Japan.
 - (3) Rent or other compensation for the use of immovable property, including

* (1) A foreign corporation is not subject to corporation tax with respect to its liquidation income.
(2) A foreign corporation for public services designated by the Minister of Finance may be exempt from income or corporation tax. There are some conditions for such designation, including the following:

(i) Principal activities of the foreign corporation must be equivalent to those of non-taxable Japanese corporations etc. such as local public entities, the Japan Red Cross Society, the Chamber of Commerce and Industry, the National Students Aid Fund, and the National Health Insurance Association.

(ii) A foreign corporation has to actually carry out its main activities in Japan and those activities must contribute to the Japanese public interest.

(iii) It must be proved that non-taxable Japanese corporations etc. of similar character are exempt from taxes in the home country of the foreign corporation on a reciprocal basis.
A foreign corporation wishing to be designated must submit to the Minister of Finance necessary documents concerning the afore-mentioned conditions.

When such a designated corporation engages in profit-making business in Japan, the income derived from such business is subject to corporation tax at the reduced rate of 22% (see 3/4, 2, a. (2)).

(3) Foreign association without juridical personality but with a representative or manager that is continuously engaged in profit-making activities through the establishment of a place of business is subject to income and corporation taxes.

rights thereon, located in Japan, royalties for the use of quarrying rights or mining rights granted under Japanese law, and rental of a bare-boat charter of a ship or of an aircraft in which the lessee is a Japanese resident or a domestic corporation.

- (4) Interest on national or local government bonds or debentures issued by domestic corporations or on deposits made with entities that have a place of business in Japan, as well as the distribution of profits from joint operation trusts or bond investment trusts represented by entities with a place of business in Japan.
 - (5) Dividends or distribution of surpluses and profits from securities investment trusts (excluding bond investment trusts) received from domestic corporations.
 - (6) Interest on loans, when the money lent is used with respect to business conducted in Japan by the debtor.
 - (7) Royalties (not depending on whether it is temporary or continuous) for the use of, or the right to use, patents (including know-how), copyrights (including the rights to use motion picture films, television films, or video-tapes), their neighboring rights, or equipment and proceeds from the sale of patents or copyrights, when such royalties or considerations are paid with respect to such properties by a person conducting business in Japan.
 - (8) Awards or similar profits related to advertisements provided in Japan.
 - (9) Annuities on life insurance, indemnity insurance, or similar contracts concluded through a place of business in Japan.
 - (10) Interest, profits, or premiums accrued from quasi-financial products such as foreign currency time deposits, gold deposit accounts, mortgage-backed securities, etc.
 - (11) Distribution of profit under a sleeping partnership contract or similar contract for the purpose of investment in business conducted in Japan.
- b.** Rules for determining the scope of income from sources within Japan, such as the principle of allocation of income from business conducted concurrently in Japan and abroad are the same as those described in 24/1, 2. b and 2. c above.

3. Classification of Foreign Corporations and Assessment of Corporation Tax and/or Income Tax on Foreign Corporations

- a.** Foreign corporations are classified, for corporation tax purposes, into the following four categories depending on the type of permanent establishment (PE) and so on:

- (1) A foreign corporation that has a branch, sub-branch, office, factory, mine, quarry, or other fixed place of business* (“subparagraph (1) PE”) in Japan.
 - (2) A foreign corporation, other than that of type (1) above, that undertakes construction, installation, or assembly activities or provides personal services for the supervision or superintendence of such activities for more than one year in Japan (“subparagraph (2) PE”).
 - (3) A foreign corporation, other than that of type (1) above, that carries out business in Japan through the following agents (“subparagraph (3) PE”):
 - (a) A person having and habitually exercising the authority to conclude contracts in Japan for, or on behalf of, the foreign corporation**, unless the activities of such foreign corporation are limited exclusively to the purchase of goods or merchandise;
 - (b) A person habitually maintaining in Japan a stock of goods or merchandise from which he or she regularly fills orders and makes deliveries on behalf of the foreign corporation;
 - (c) A person habitually securing orders, negotiating, or performing other important activities in Japan for concluding contracts, exclusively or almost exclusively for, or on behalf of, the foreign corporation.
 - (4) A foreign corporation other than any of (1) to (3) above (a foreign corporation without PE).
- b.** e forms of tax treatment differs according to the type of foreign corporation also see 5 below):
- (1) The foreign corporation mentioned in a. (1) above is subject to corporation tax on its total Japanese-source income.
 - (2) A foreign corporation falling under the category of (2) or (3) above is subject to corporation tax on its total income in (1) to (3) in 2. a above, and on such parts of its income in (4) to (11) in 2. a above, as is attributable to business conducted through a permanent establishment in Japan in the form of construction, installation, or assembly activities or through agents mentioned in (3) above. Such parts of its income in (4) to (11) in 2. a that are not attributable to the business conducted through a permanent establishment are subject only to withholding “separate income taxation,” i.e., taxation at a flat rate of 20% (or 7%, 15%) of gross revenue.
 - (3) In the case of the foreign corporation mentioned in (4) above, corpora-

* “Fixed place of business” in this respect does not include the use of facilities solely for the purchase and the storage of goods or merchandise belonging to the foreign corporation, nor a place of business used solely for the purchase of goods or merchandise, or for advertising, publicity, marketing research, or business activities of an auxiliary character for the foreign corporation.

** However, a person who engages in the same kind of business as that of the foreign corporation and exercises the authority to conclude contracts for them because of the very nature of such (international) business is not considered an agent for this category.

tion tax is imposed only on parts of its income of (1)* in 2. a above, and its total income in (2) and (3) in 2. a above, while income in (4) to (11) in 2. a above of such a foreign corporation is always subject only to 20% (or 7%, 15%) withholding of “separate income taxation.”

4. Principle of Tax Calculation

a. Taxable income of a foreign corporation is calculated on the basis of its income from sources within Japan. The provisions in laws and cabinet orders for the calculation of taxable income applicable to domestic Corporations are likewise applied, *mutatis mutandis*, to foreign corporations. Necessary modifications to the rules for such calculation, however, are provided in the Cabinet Order which follows:

- (1) Costs of sales and overhead expenses of a foreign corporation are allowed as deductions to the extent that such costs are reasonably allocated to its business conducted in Japan on the basis of receipts, expenditures, value of assets situated in Japan, or other relevant factors.
- (2) The method of inventory valuation prescribed under the Corporation Tax Law is applied to inventories of a foreign corporation that are actually kept in Japan.
- (3) A depreciation deduction is granted for the assets of a foreign corporation actually located in Japan.
- (4) Corporation taxes imposed by a foreign country (including any local taxes on income) to be paid by a foreign corporation, are not deductible as expenses even for such portions of the tax that are imposed on its income from sources within Japan.
- (5) A reserve for bad debts may be provided for the credits of a foreign corporation maintained in connection with its business conducted in Japan.
- (6) Upon closing of all permanent establishments situated in Japan, a foreign corporation loses, in the accounting period of such closure, the benefits of tax-free reserves and tax deferment through special treatment of revenues and expenses with respect to installment sales or long-term construction contracts, etc.

* The part of income of (1) in 2. a above that is taxable for a foreign corporation without PE mentioned in (4) consists of income from the following items as well as occasional income arising in Japan:

- (1) Utilization or holding of assets situated in Japan
- (2) Sale or disposal of immovable properties (including rights thereon) located in Japan
- (3) Disposal or cutting of timber standing in Japan
- (4) Transfer of forestalled shares (including shares designated by the Stock Exchange as “special information issues”) of, or substantial participation in, a domestic corporation
- (5) Capital gains of equities of Real estate cooperation and special trust of Real Estate.

- b.** Special forms of tax treatment provided by the Special Taxation Measures Law, with respect to the calculation of the tax base for corporation tax purposes, are, as a rule, applicable to foreign corporations.

The provisions of the Law stipulating that certain categories of interest are not subject to income tax are also applicable to foreign corporations (see 24/1, 5. (2)).

- c.** The rate of corporation tax on ordinary foreign corporations is 30% of the income for each accounting period. However, the tax rate applied to foreign corporations with capital no more than ¥100 million is reduced to 22% for those with annual income of no more than ¥8 million.
- d.** Income tax credit with respect to corporation tax is granted to a foreign corporation for the income tax withheld on its income of types (2) to (11) in 2. a above (exclusive of such income that is subject only to “separate income taxation” and certain dividends) (see 3 above).

5. Withholding Income Tax at the Source

- a.** Anyone who has income classified under items 24/1, 2. a. (2) to (9) and (11) to (14) in Japan form a foreign corporation is required to withhold income tax at the rate of 20%* (10% on income which is described in 24/1, 2. a.(3)) and to pay the tax thus withheld to the government before the 10th day of the month following the month of withholding. If the payment is made abroad (e.g., through a paying agent located abroad), the payer must withhold and pay such tax, if the original payer is a resident, a domestic corporation, a nonresident having temporary residence, a permanent establishment in Japan, or a foreign corporation having a permanent establishment in Japan. In the latter case, payment of the tax to the government must be made before the end of the month following the month of payment.

In cases where such income is not subject to corporation tax, the income tax paid by means of withholding constitutes the final tax liability thereon.

Note: Redemption premiums on certain debentures issued at a discount are subject to income tax at the rate of 18% (or 16%).**

- b.** If the recipient foreign corporation has a permanent establishment in Japan, withholding tax may be exempted for the following types of income, provided that the recipient obtains from the Tax Office a certificate stating that such

* With respect to income categories (6) and (13) in 24/1 2.a above and income from securities investment trusts, withholding of income tax at the source is at the rate of 15%. (And 7% for the income from certain listed stocks in (7) of 24/1 2.a)

** If the maximum rate on redemption premiums is set at 10% by a double taxation convention, 10% is applicable.

income is subject to corporation tax, together with the following income types from business in Japan, and presents it to the payer of income:

- (1) Income classified under items (2) to (5), (8), (9), (11) and (12) in 24/1, 2. a that is received by a foreign corporation of type (1) in 3 above.
 - (2) Income mentioned in (1) above that is received by a foreign corporation of type (2) or (3) in 3 above and is attributable to a permanent establishment through which its business is conducted in Japan.
- c.** For income from business that consists of providing personal services by a foreign corporation that conducts such business in Japan, if a withholding has already been made, the foreign corporation operating such business is not required to withhold income tax when it pays, out of such receipts, salaries or other remunerations to individual nonresidents actually performing such personal services.

6. Special Rules for Accounting Periods

If a foreign corporation with a permanent establishment in Japan closes that permanent establishment (whether or not it still maintains another type of permanent establishment as mentioned in 3. a above) during the accounting period concerned, the date of closing is deemed to be the end of that accounting period and a new accounting period begins on the following day.

For a foreign corporation having no permanent establishment but carrying out the business of providing personal services (mentioned in 2. a. (2) above) in Japan, the day of commencement or discontinuance of such business during an accounting period is regarded as the beginning of a new accounting period or the end of the previous accounting period.

7. Filing of Returns

Generally speaking, the rules governing the filing of returns for foreign corporations are the same as those for domestic corporations. With respect to a foreign corporation that has closed all of its permanent establishments in Japan without appointing and reporting to the tax authorities its tax agent in Japan or that has discontinued its business of providing personal services in Japan, the Corporation Tax Law specifically provides as follows:

- (1) A corporation tax return must be filed by the regular due date or the date of closure or discontinuance, whichever is earlier. In such an event, neither an extension of the time limit for filing a return nor postponement of tax payment is allowed.
- (2) If the date of closure or discontinuance is prior to the due date for filing its

interim return, interim return is not required.

8. Jurisdiction over Taxation Matters of Foreign Corporations

The Tax Office having jurisdiction over taxation matters of a foreign corporation is determined by, in order, the following:

- (1) Place of the foreign corporation's permanent establishment in Japan.
- (2) Location of the foreign corporation's immovable properties in Japan from which income of type (3) in 2. a above (excluding rental from a bare boat or full charter) accrues.
- (3) Place that has hitherto been determined under (1) or (2) above.
- (4) Place that the corporation has selected for filing a return, making a claim, etc.
- (5) Place under the jurisdiction of the Kojimachi Tax Office in Tokyo.

24/3 Tax Treaties

1. Japan's tax treaties

Japan has concluded 45 treaties (applicable to 56 countries) for avoiding double taxation and preventing fiscal evasion with respect to taxes on income and a convention for avoiding double taxation and preventing fiscal evasion with respect to taxes on estates, inheritances, and gifts with the United States of America.

Tax Treaties of Japan

(As of 2006)

Country	Date of Signature	Date to Take Effect	Taxes Covered
1. United States of America	(0)1954. 4.16	1955. 4. 1	Japan: Income tax Corporation tax U.S.A.: Federal income tax
(1) For tax on income	(1)1957. 3.23	1957. 9. 9	
	(2)1960. 5. 7	1964. 9. 2	
	(3)1962. 8.14	1965. 5. 6	
	(R)1971. 3. 8	1972. 7. 9	
	(R)2003.11. 6	2004. 3.30	Japan: Inheritance tax (including the gift tax) U.S.A.: Federal income tax
(2) For tax on estates, inheritances and gifts	1954. 4.16	1955. 4. 1	

Tax Treaties of Japan (Continued)

Country	Date of Signature	Date to Take Effect	Taxes Covered
2. Sweden	(0)1956.12.12 (1)1964. 4.15 (R)1983. 1.21 (1)1999. 2.19	1957. 6. 1 1965. 5.25 1983. 9.18 1999.12.25	Japan: Income tax Corporation tax Inhabitants tax Sweden: National income tax, including the withholding tax on dividends, the income tax on nonresidents, the income tax on non-resident artists and athletes, the municipal income tax, and, the tax on means intended for expansion purposes)
3. Pakistan	(0)1959. 2.17 (1)1960. 6.28	1959. 5.14 1961. 8. 1	Japan: Income tax Corporation tax Pakistan: Income tax Super tax Business profits tax
4. Norway	(0)1950. 2.21 (R)1967. 5.11 (R)1992. 3. 4	1959. 9.15 1968.10.25 1992.12.16	Japan: Income tax Corporation tax inhabitants tax Norway: National income tax County municipal income tax Municipal income tax National contributions to the Tax Equalization Fund National income tax on the exploration and exploitation of submarine petroleum resources and activities and related work, including pipeline transport of petroleum produced National dues on remunerations to nonresident artists
5. Denmark	(0)1959. 3.10 (R)1968. 2. 3	1959. 4.24 1968. 7.26	Japan: Income tax Corporation tax Inhabitants tax Denmark: Ordinary income tax for the State Municipal income tax Old-age pension attribution Seamen's tax Special income tax Church tax

Tax Treaties of Japan (Continued)

Country	Date of Signature	Date to Take Effect	Taxes Covered
6. India	(0)1960. 1. 5 (1)1969. 4. 8 (R)1989. 3. 7 (1)2006. 2.24	1960. 6.13 1970.11.15 1989.12.29 2006. 6.28	Japan: Income tax Corporation tax India: Income tax (including weighted tax)
7. Singapore	(0)1961. 4.11 (R)1971. 1.29 (1)1981. 1.14 (R)1994. 4. 9	1961. 9. 5 1971. 8. 3 1981. 6.23 1995. 4.28	Japan: Income tax Corporation tax Inhabitants tax Singapore: Income tax
8. Austria	(0)1961.12.20	1963. 4. 4	Japan: Income tax Corporation tax Austria: Income tax (Einkommensteuer) Corporation tax (Körperschaftsteuer) Contribution from income for the promotion of residential building and for the equalization of family burdens (Beitrag vom Einkommen zur Förderung des Wohnbaues und für Zwecke des Familienlastenausgleiches)
9. United Kingdom*	(0)1962. 9. 4 (R)1969. 2.10 (1)1980. 2.14 (R)2006. 2. 2	1963. 4.23 1970.12.25 1980.10.31 (not in effect)	Japan: Income tax Corporation tax Inhabitants tax United Kingdom: Income tax (including sur-tax) Corporation tax Capital gains tax Taxes described above are subject to new tax treaty.
10. New Zealand	(0)1963. 1.30 (1)1967. 3.22	1963. 4.19 1967. 9.30	Japan: Income tax Corporation tax New Zealand: Income tax Excess retention tax
11. Thailand	(0)1963. 3. 1 (R)1990. 4. 7	1963. 7.24 1990. 8.31	Japan: Income tax Corporation tax Thailand: Income tax Petroleum income tax
12. Malaysia	(0)1963. 6. 4 (R)1970. 1.30 (R)1999. 2.19	1963. 8.21 1970.12.23 1999.12.31	Japan: Income tax Corporation tax Local inhabitants tax Malaysia: Income tax Petroleum income tax

Tax Treaties of Japan (Continued)

Country	Date of Signature	Date to Take Effect	Taxes Covered
13. Canada	(0)1964. 9. 5 (R)1986. 5. 7 (1)1999. 2.19	1965. 4.30 1987.11.14 2000.12.14	Japan: Income tax Corporation tax Canada: Income tax imposed by the Government of Canada
14. France	(0)1964.11.27 (1)1981. 3.10 (R)1995. 3. 3	1965. 8.22 1981.10.14 1996. 3.24	Japan: (i) l'impôt sur le revenu; (ii) l'impôt sur les sociétés; (iii) les impôts sur les habitants; France: (i) l'impôt sur le revenu; (ii) l'impôt sur les sociétés; (iii) l'imposition forfaitaire annuelle des sociétés; y compris toutes retenues à la source , tous précomptes et tous versements anticipés afférents à ces impôts;
15. Germany	(0)1966. 4.22 (1)1979. 4.17 (2)1983. 2.17	1967. 6. 9 1980.11.10 1984. 5. 4	Japan: Income tax Corporation tax Inhabitants tax Enterprise tax Germany: Income tax Corporation tax Trade tax Capital tax
16. Brazil	(0)1967. 1.24 (1)1976. 3.23	1967.12.31 1977.12.29	Japan: Income tax Corporation tax Brazil: Federal income tax
17. Sri Lanka	1976.12.12	1968. 9.22	Japan: Income tax Corporation tax Sri Lanka: Income tax
18. Belgium	(0)1968. 3.28 (1)1988.11. 9	1970. 4.16 1990.11.16	Japan: Income tax Corporation tax Inhabitants tax Belgium: (i) Individual income tax (l'impôt des personnes physiques) (ii) Corporate income tax (l'impôt des sociétés) (iii) Income tax on legal entities (impôt des personnes morales)

Tax Treaties of Japan (Continued)

Country	Date of Signature	Date to Take Effect	Taxes Covered
			<p>(iv) Income tax on nonresidents (l'impôt des nonrésidents)</p> <p>(v) Prepayments and additional prepayments (les précomptes et compléments de précomptes)</p> <p>(vi) Surcharge (centimes additionnels) on any of the taxes referred to in (i) to (v) above including the communal supplement to individual income tax (taxe communale additionnelle à l'impôt des personnes physiques)</p>
19. Arab Republic of Egypt	1968. 9. 3	1969. 8. 6	<p>Japan: Income tax Corporation tax Inhabitants tax</p> <p>Egypt: Tax on income derived from immovable property (including land tax, buildings tax, and the ghaffir tax)</p> <p>Tax on income from movable capital</p> <p>Tax on commercial and industrial profits</p> <p>Tax on wages, salaries, indemnities and pensions</p> <p>Tax on profits from liberal professions and all other non-commercial professions</p> <p>General income tax</p> <p>Defense tax</p> <p>National security tax</p> <p>Supplementary tax imposed as a percentage of taxes mentioned above or otherwise</p>

Tax Treaties of Japan (Continued)

Country	Date of Signature	Date to Take Effect	Taxes Covered
20. Australia	1969. 3.20	1970. 7. 4	Japan: Income tax Corporation tax Australia: Commonwealth income tax, including additional tax upon the undistributed amount of distributable income of a private company
21. Italy	(0)1969. 3.20 (1)1980. 2.14	1973. 3.17 1982. 1.28	Japan: Income tax Corporation tax Inhabitants tax Italy: Personal income tax (imposta sul reddito delle persone fisiche) Corporate income tax (imposta sul reddito delle persone giuridiche) Local income tax (imposta locale sui redditi)
22. Zambia	1970. 2.19	1971. 1.23	Japan: Income tax Corporation tax Inhabitants tax Zambia: Income tax Personal levy
23. Netherlands	(0)1970. 3. 3 (1)1992. 3. 4	1970.10.23 1992.12.16	Japan: Income tax Corporation tax Inhabitants tax Netherlands: Income tax Wage tax Corporation tax Dividend tax
24. Republic of Korea	(0)1970. 3. 3 (R)1998.10. 8	1970.10.29 1999.11.22	Japan: Income tax Corporation tax Inhabitants tax Korea: The income tax, the corporation tax, the special tax for rural development surtaxed directly or indirectly on the tax base of the income tax or the corporation tax, and the local inhabitants tax

Tax Treaties of Japan (Continued)

Country	Date of Signature	Date to Take Effect	Taxes Covered
25. Switzerland	1971. 1.19	1971.12.26	Japan: Income tax Corporation tax Inhabitants tax Switzerland: Federal, cantonal, and communal taxes on income (total income, earned income, income from capital, industrial and commercial profits, capital gains, and other items of income)
26. Finland	(0)1972. 2.29 (1)1991. 3. 4	1972.12.30 1991.12.28	Japan: Income tax Corporation tax Inhabitants tax Finland: State income tax Communal income tax Church tax Withholding tax on non-residence income
27. Ireland	1974.1.18	1974.12. 4	Japan: Income tax Corporation tax Inhabitants tax Ireland: Income tax (including surtax) Corporation profit tax
28. Spain	1974. 2.13	1974.11.20	Japan: Income tax Corporation tax Inhabitants tax Spain: General income tax on individuals General income tax on corporation, including a special charge of 4 per cent established by Article 104, Law 41 on 11 June 1964 Following Prepayments: tax on rural land, tax on urban land, tax on earned income, tax on income from capital, and tax on business and industrial activities In Sahara, the income tax

Tax Treaties of Japan (Continued)

Country	Date of Signature	Date to Take Effect	Taxes Covered
			<p>(on earned income and on income from capital) and tax on profits of enterprises</p> <p>Surface royalty, tax on gross yield and special tax on corporation profits, regulated by Law 26 in December 1958 (applicable to enterprises engaged in prospecting and exploiting oil wells)</p> <p>Local tax on income</p>
29. Romania	1976. 2.12	1978. 4. 9	<p>Japan: Income tax</p> <p>Corporation tax</p> <p>Inhabitants tax</p> <p>Romania: Tax on wages or salaries and income from literary, artistic, or scientific works, as well as income derived from collaborations for publications, shows, examinations, and similar activities</p> <p>Tax on incomes of non-resident individuals and corporate bodies</p> <p>Tax on income of mixed companies</p> <p>Tax on income derived from productive activities such as trade, free professions, as well as income derived from enterprises other than state enterprises and mixed companies</p> <p>Tax on income derived from the leasing of buildings and land</p> <p>Tax on income derived from agricultural activities</p> <p>Tax on income from consumption cooperatives and handicraft cooperatives</p>

Tax Treaties of Japan (Continued)

Country	Date of Signature	Date to Take Effect	Taxes Covered
30. Czech-Slovakia**	1977.10.11	1978.11.25	Japan: Income tax Corporation tax Inhabitants tax Czechoslovakia: Tax on profits Wage tax Tax on income from literary and artistic activities Agricultural tax Tax on population income House tax
31. Philippines	1980. 2.13	1980. 7.20	Japan: Income tax Corporation tax Philippines: Philippines income tax
32. Hungary	1980. 2.13	1980.10.25	Japan: Income tax Corporation tax Inhabitants tax Hungarian People's Republic: Income tax Profit tax Special corporation tax Contribution to communal development imposed with respect to income taxes Levy on dividends and profit distributions of commercial companies
33. Poland	1980. 2.20	1982.12.23	Japan: Income tax Corporation tax Inhabitants tax Poland: Income tax (podatek dochodowy) Tax on wages or salaries (podatek od wynagrodzen') Surcharge on income tax or on tax on wages or salaries (podatek wyrównawczy)
34. Indonesia	1982. 3. 3	1982.12.31	Japan: Income tax Corporation tax Indonesia: Income tax (Pajak Pendapatan) Company tax (Pajak

Tax Treaties of Japan (Continued)

Country	Date of Signature	Date to Take Effect	Taxes Covered
			Perseroan) including any withholding tax, prepayment, or ad vance payment with respect to the aforementioned taxes; Tax on interest, dividends, and royalties (Pajak Atas Bunga, Dividen dan Royalty)
35. China	1983. 9. 6	1984. 6.26	Japan: Income tax Corporation tax Inhabitants tax China: Individual income tax Income tax on joint ventures using Chinese and foreign investment Income tax concerning foreign enterprises Local income tax
36. U.S.S.R.***	1986. 1.18	1986.11.27	Japan: Income tax Corporation tax Inhabitants tax USSR: Individual income tax Income tax on foreign legal persons
37. Bangladesh	1991. 2.28	1991. 6.15	Japan: Income tax Corporation tax Bangladesh: Income tax
38. Bulgaria	1991. 3. 7	1991. 8. 9	Japan: Income tax Corporation tax Inhabitants tax Bulgaria: Tax on total income Tax on profits
39. Luxembourg	1992. 3. 5	1992.12.27	Japan: Income tax Corporation tax Inhabitants tax Luxembourg: Income tax on individuals Corporation tax Tax on fees for directors of companies Capital tax, local business tax

Tax Treaties of Japan (Continued)

Country	Date of Signature	Date to Take Effect	Taxes Covered
40. Israel	1993. 3. 8	1993.12.24	Japan: Income tax Corporation tax Inhabitants tax Israel: Tax imposed according to the Income Tax Ordinance and its adjunct laws Tax imposed upon the alienation of property according to the Land Appreciation Tax Law
41. Turkey	1993. 3. 8	1994.12.28	Japan: Income tax Corporation tax Inhabitants tax Turkey: Income tax Corporation tax Taxes imposed on income tax and corporation tax
42. Viet Nam	1995.10.24	1995.12.31	Japan: Income tax Corporation tax Inhabitants tax Viet Nam: Income tax, profit tax, profit remittance. tax, foreign contractor tax (to the extent considered to be tax imposed on profit) Foreign petroleum subcontractor tax (to the extent considered to be tax imposed on profit) Royalty tax
43. Mexico	1996. 4. 9	1996.11. 6	Japan: Income tax Corporation tax Inhabitants tax Mexico: Income tax
44. South Africa	1997. 3. 7	1997.11. 5	Japan: Income tax Corporate tax Inhabitant tax South Africa: Normal tax Secondary tax on corporation

Note: (0) in order of their date of signature of original convention, (1) first amendment, (2) second amendment, (3) third amendment, and overall revision

sion, respectively.

- * Original convention is applicable to the Fiji Islands.
- ** Applicable to the Czech republic and Slovakia at this time.
- *** Applicable to Russia, Kyrgyz, Georgia, Tadzhikistan, Uzbekistan, Turkmenistan, Ukraine, Armenia, Belarus, Moldova and Azerbaijan.

2. Contents of Treaties

a. Taxation of Business Profits

According to conventions, a foreign enterprise is not subject to tax on its business income in Japan unless it has a permanent establishment in Japan. The concept of “permanent establishment” varies slightly depending on the convention. It is, of course, not possible to describe in detail all of the provisions. As a rule, however, the term “permanent establishment” means as follows:

- (1) a fixed place, such as a place of management, a branch, an office, a factory, a workshop, etc., in which an enterprise conducts business;
- (2) a project for construction, installation, etc. conducted for more than twelve months; or
- (3) an agency that has and habitually exercises the authority to conclude contracts in the name of the foreign enterprise.

The following are not considered permanent establishments:

- (a) business conducted through a general commission agent or broker acting in his or her name and in the ordinary course of his or her business as such and;
- (b) the maintenance of a fixed place of business solely for the purchase of goods or merchandise for the foreign enterprise.

If an enterprise has a permanent establishment in the other signatory nation, it is subject to tax in the country on those business profits attributable to the permanent establishment. The only exceptions are conventions with Pakistan under which enterprises of those countries, if they have a permanent establishment in the other signatory nation, are subject to tax on their entire income derived in the nation.

b. Taxation of Investment Income (Dividends, Interest, and Royalties)

For most conventions, investment income may be taxed at reduced rates or is exempt from tax in Japan if the income received by the nonresident or foreign corporation investors is not attributable to the permanent establishment situated in Japan.

Taxation of Investment Income

(1) Dividends

Country	Maximum Tax Rate		Notes
	(a) For dividends from portfolio investment	(b) For dividends paid by a subsidiary	
1. United States of America	10%	5% or exempt as to certain conditions	
2. Sweden	15%	5% or exempt as to certain dividends	
3. Denmark	15%	10%	
4. Pakistan	No provision	Japan: 15% Pakistan: 6.25%	Maximum tax rate of 6.25% is applied only to dividends paid to certain Japanese corporations by a Pakistani company engaged in an industrial undertaking.
5. Norway	15%	5%	
6. India	10%	No provision	
7. Singapore	Japan: 15% Singapore: Nontaxable	Japan: 5% Singapore: Nontaxable	
8. Austria	20%	10%	
9. United Kingdom	10%	Certain dividend: exempt Other: 5%	
10. New Zealand	15%	No provision	
11. Thailand	No provision	20% 15%*	*In the case of dividends paid by a corporation engaged in an industrial undertaking
12. Malaysia	Japan: 15% Malaysia: Nontaxable	Japan: 5% Malaysia: Nontaxable	
13. Canada	15%	5%	
14. France	15%	5% (in the case of a qualified resident, exempt.)	

XXIV Taxation of Nonresidents and Foreign Corporations

Country	Maximum Tax Rate		Notes
	(a) For dividends from portfolio investment	(b) For dividends paid by a subsidiary	
15. Germany	15%	Japan: 10% Germany: No provision	
16. Brazil	12.5%	No provision	
17. Sri Lanka	Japan: 20% Sri Lanka:6%*	No provision	*6% of additional tax is imposed on corporations resident in Japan
18. Arab Republic of Egypt	Japan: 15% Egypt:—(20%)	No provision	Figure in parenthesis is applied only to general income tax pertinent to individuals
19. Belgium	15%	Japan: 10% Belgium: 5%	
20. Australia	15%	No provision	
21. Netherlands	15%	5%	
22. Republic of Korea	15%	5% (10% until 2003)	
23. Zambia	Exempt	Exempt	
24. Switzerland	15%	10%	
25. Finland	15%	10%	
26. Italy	15%	10%	
27. Spain	15%	10%	
28. Ireland	Japan: 15% Ireland: Nontaxable	Japan: 10% Ireland: Nontaxable	
29. Romania	10%	No provision	
30. Czech-Slovakia	15%	10%	
31. Philippines	25%	10%	For (a), a tax rate of 10% is applied to the dividends paid by certain Philippine companies engaged in preferred pioneer areas of investment.
32. Hungary	10%	No provision	
33. Poland	10%	No provision	

XXIV Taxation of Nonresidents and Foreign Corporations

Country	Maximum Tax Rate		Notes
	(a) For dividends from portfolio investment	(b) For dividends paid by a subsidiary	
34. Indonesia	15%	10%	
35. China	10%	No provision	
36. U.S.S.R	15%	No provision	
37. Bangladesh	15%	10%	
38. Bulgaria	15%	10%	
39. Luxembourg	15%	5%	
40. Israel	15%	5%	
41. Turkey	15%	10%	For Turkey, the tax rates shall be 20 per cent for a) and 15 percent for b), respectively, where the amount of Turkish tax imposed on the income of the company paying dividends is less than 40 per cent of such income derived in the accounting period ending immediately before the date when such dividends become payable.
42. Viet Nam	10%	No provision	For (b), portioners are exempt if they are listed corporations and more than half of their stocks are held by the government and/or individual residents.
43. Mexico	15%	5%	
44. South Africa	15%	5%	

(2) Interest

Country	(a) Maximum tax rate	(b) Interest received by the Bank of Japan	(c) Redemption premium	Notes
1. United States of America	Exempt if the beneficial owner is a bank; 10% for the rest	Exempt	Included in the definition of interest	
2. Sweden	10%	No provision	Included in the definition of interest	
3. Denmark	10%	No provision	Included in the definition of interest	
4. Pakistan	30%	Exempt	No provision	Interest from certain sources shall be exempt.
5. Norway	10%	Exempt	Included in the definition of interest	
6. India	10%	Exempt	Included in the definition of interest	
7. Singapore	10%	Exempt	Included in the definition of interest	
8. Austria	10%	No provision	No provision	
9. United Kingdom	Exempt if the beneficial owner is a bank; 10% for the rest	Exempt	Included in the definition of interest	
10. New Zealand	No provision	No provision	No provision	
11. Thailand	10% if the beneficial owner is a financial institution; 25% for the rest (applicable to corporations only)	Exempt	Included in the definition of interest	

XXIV Taxation of Nonresidents and Foreign Corporations

Country	(a) Maximum tax rate	(b) Interest received by the Bank of Japan	(c) Redemption premium	Notes
12. Malaysia	10%	Exempt	Included in the definition of interest	
13. Canada	10%	Exempt	Included in the definition of interest	
14. France	10%	Exempt	Included in the definition of interest	Interest arising from the sale on credit of any equipment or merchandise is exempt under certain conditions.
15. Germany	10%	Exempt	No provision	Interest on bonds is exempt from tax if the payments of principal or interest of such bonds are guaranteed by the Government of either State.
16. Brazil	12.5%	Exempt	No provision	
17. Sri Lanka	No provision	Interest received by banking institution is exempt from tax in the source State.	No provision	
18. Arab Republic of Egypt	No provision	No provision	No provision	
19. Belgium	10%	No provision	No provision	
20. Australia	10%	No provision	No provision	
21. Netherlands	10%	Exempt	No provision	
22. Republic of Korea	10%	Exempt	Included in the definition of interest	
23. Zambia	10%	Exempt	Included in the definition of interest	
24. Switzerland	10%	Exempt	No provision	

XXIV Taxation of Nonresidents and Foreign Corporations

Country	(a) Maximum tax rate	(b) Interest received by the Bank of Japan	(c) Redemption premium	Notes
25. Finland	10%	No provision	No provision	
26. Italy	10%	No provision	Included in the definition of interest	
27. Spain	10%	No provision	No provision	
28. Ireland	10%	No provision	Included in the definition of interest	
29. Romania	10%	Exempt	Included in the definition of interest	
30. Czech- Slovakia	10%	10%	Included in the definition of interest	
31. Philip- pines	15%	Exempt	Included in the definition of interest	Maximum tax rate of 10% is applied to a) interest on bonds or debentures; and b) interest paid by a certain Philippine company en- gaged in preferred pio- neer areas of invest- ment.
32. Hungary	10%	Exempt	Included in the definition of interest	
33. Poland	10%	Exempt	Included in the definition of interest	
34. Indonesia	10%	Exempt	Included in the definition of interest	
35. China	10%	Exempt	Included in the definition of interest	
36. U.S.S.R.	10%	Exempt	Included in the definition of interest	

XXIV Taxation of Nonresidents and Foreign Corporations

Country	(a) Maximum tax rate	(b) Interest received by the Bank of Japan	(c) Redemption premium	Notes
37. Bangla- desh	10%	Exempt	Included in the definition of interest	
38. Bulgaria	10%	Exempt	Included in the definition of interest	
39. Luxem- bourg	10%	Exempt	Included in the definition of interest	
40. Israel	10%	Exempt	Included in the definition of interest	
41. Turkey	10% for in- terest re- ceived by financial in- stitutions and 15% for the rest	Exempt for the Bank of Japan	Included in the definition of interest	
42. Viet Nam	10%	Exempt	Included in the definition of interest	
43. Mexico	10% for banks and 15% for the rest	Exempt	Included in the definition of interest	
44. South Africa	10%	Exempt	Included in the definition of interest	

(3) Royalties

Country	(a) Maximum tax rate	(b) Proceeds arising from the alienation of patents, copyrights, etc.	(c) Receipts from a bareboat charter of ships or aircraft	Notes
1. United States of America	Exempt	No provision	No provision	
2. Sweden	10%	The maximum tax rate of 10% mentioned in (a) is applied.	Included in the definition of royalties	
3. Denmark	10%	The maximum tax rate of 10% mentioned in (a) is applied.	Included in the definition of royalties	
4. Pakistan	Exempt (if no PE)	No provision	No provision	
5. Norway	10%	The maximum tax rate of 10% mentioned in (a) is applied.	No provision	Certain payments (i.e., those received as a consideration for the use of, or the right to use, industrial, commercial, or scientific equipment as well as receipts mentioned in (c)) are considered business income.
6. India	10%	No provision	No provision	This provision is also applied to “fees for technical services.”
7. Singapore	10%	The maximum tax rate of 10% mentioned in (a) is applied.	No provision	
8. Austria	10%	The maximum tax rate of 10% mentioned in (a) is applied.	No provision	

XXIV Taxation of Nonresidents and Foreign Corporations

Country	(a) Maximum tax rate	(b) Proceeds arising from the alienation of patents, copyrights, etc.	(c) Receipts from a bareboat charter of ships or aircraft	Notes
9. United Kingdom	Exempt	No provision	No provision	
10. New Zealand	No provision	No provision	No provision	
11. Thailand	15%	The maximum tax rate of 15% mentioned in (a) is applied.	No provision	Certain payments (i.e., those received in consideration for the use of cinematic film) are not included in the definition of royalties.
12. Malaysia	10%	The maximum tax rate of 10% mentioned in (a) is applied.	Included in the definition of interest	
13. Canada	10%	No provision	No provision	
14. France	10%	The maximum tax rate of 10% mentioned in (a) is applied to the proceeds excluding the gains from a genuine alienation of a patent or similar property.	No provision	
15. Germany	10%	The maximum tax rate of 10% mentioned in (a) is applied to the proceeds excluding the gains from a genuine alienation of a patent or similar property.	No provision	
16. Brazil	12.5%	No provision	No provision	Lower rates are applied for the following categories of Royalties:

XXIV Taxation of Nonresidents and Foreign Corporations

Country	(a) Maximum tax rate	(b) Proceeds arising from the alienation of patents, copyrights, etc.	(c) Receipts from a bareboat charter of ships or aircraft	Notes
				1) For royalties arising from the use of, or the right to use, trademarks 25% 2) For royalties arising from the use of, or the right to use copyright of cinematograph films, etc. 15%
17. Sri Lanka	No provision (But the tax chargeable under domestic laws is reduced by an amount equal to 50% thereof.)	No provision	No provision	Any royalty receivable in consideration for the use of, or the right to use, any copyright or cinematic films is exempt.
18. Arab Republic of Egypt	15%	No provision	No provision	Royalties for cinematic films are subject to taxation under the domestic laws of each country.
19. Belgium	10%	The maximum tax rate of 10% mentioned in (a) is applied to the proceeds, excluding gains from a genuine alienation of a patent or similar property.	Included in the definition of royalties	
20. Australia	10%	No provision	No provision	
21. Netherlands	10%	The maximum tax rate of 10% mentioned in (a) is applied to	No provision	

XXIV Taxation of Nonresidents and Foreign Corporations

Country	(a) Maximum tax rate	(b) Proceeds arising from the alienation of patents, copyrights, etc.	(c) Receipts from a bareboat charter of ships or aircraft	Notes
		the proceeds, excluding gains from a genuine alienation of a patent or similar property.		
22. Republic of Korea	10%	The maximum tax rate of 10% mentioned in (a) is applied.	Included in the definition of royalties	
23. Zambia	10%	No provision	No provision	
24. Switzerland	10%	The maximum tax rate of 10% mentioned in (a) is applied to the proceeds, excluding gains from a genuine alienation of a patent or similar property.	No provision	
25. Finland	10%	The maximum tax rate of 10% mentioned in (a) is applied.	No provision	
26. Italy	10%	No provision	No provision	
27. Spain	10%	The maximum tax rate of 10% mentioned in (a) is applied to proceeds other than gains from genuine alien-	No provision	

XXIV Taxation of Nonresidents and Foreign Corporations

Country	(a) Maximum tax rate	(b) Proceeds arising from the alienation of patents, copyrights, etc.	(c) Receipts from a bareboat charter of ships or aircraft	Notes
		ation of a patent or si- milar prop- erty.		
28. Ireland	10%	No provision	No provision	
29. Romania	Cultural ro- yalties; 10% Industrial royalties; 15%	No provision	No provision	
30. Czech- Slovakia	Cultural ro- yalties; exe- mpt Industrial royalties; 10%	No provision	No provision	
31. Philip- pines	25%	No provision	No provision	Lower rates are applied to the following catego- ries of royalties: 1) for royalties arising from the use of, or the right to use cinematic films etc. – 15% 2) for royalties paid by a company engaged in preferred pioneer ar- eas of investment – 10%
32. Hungary	Cultural roy- alties: exempt; Industrial ro- yalties: 10%	No provision	No provision	
33. Poland	Cultural roy- alties: exempt; Industrial ro- yalties: 10%	No provision	No provision	

XXIV Taxation of Nonresidents and Foreign Corporations

Country	(a) Maximum tax rate	(b) Proceeds arising from the alienation of patents, copyrights, etc.	(c) Receipts from a bareboat charter of ships or aircraft	Notes
34.Indonesia	10%	No provision	No provision	
35. China	10%	No provision	No provision	
36. U.S.S.R.	Cultural roy- alties: exempt; Industrial ro- yalties: 10%	No provision	No provision	
37.Banglade sh	10%	Maximum tax rate of 10% mentioned in (a) is applied	No provision	
38. Bulgaria	10%	Maximum tax rate of 10% mentioned in (a) is applied	No provision	
39.Luxembo urg	10%	No provision	Included in the definition of royalties	
40. Israel	10%	Maximum tax rate of 10% mentioned in (a) is applied	Included in the definition of royalties	
41. Turkey	10%	Maximum tax rate of 10% mentioned in (a) is applied	Include in the definition of royalties	
42. Viet Nam	10%	Maximum tax rate of 10%, is applied to tr- ansfer profits except those made through gene vine transfers of patents or similar prop- erties (prop- erty rights)	No provision	

Country	(a) Maximum tax rate	(b) Proceeds arising from the alienation of patents, copyrights, etc.	(c) Receipts from a bareboat charter of ships or aircraft	Notes
43. Mexico	10%	Maximum tax rate of 10% mentioned in (a) is applied	No provision	
44. South Africa	10%	Maximum tax rate of 10% mentioned in (a) is applied	Included in the definition of royalties	

c. Taxation of Personal Services

All treaties provide that remuneration for personal services received by residents in one signatory nation is taxable in the other signatory nation if the services are rendered in the latter. A resident of a treaty partner who is temporarily present (for a period not exceeding 183 days in the calendar or fiscal year, etc.) and rendering services in Japan for or on behalf of an employer who is not a resident of Japan is exempt from Japanese tax on remunerations for those services. This exemption does not apply to public entertainers except in certain cases. Under most of the treaties, income derived from professional services or other independent activities is not taxable unless the person has a fixed base in Japan. The treaties grant certain exemptions for the income of students, business apprentices, and professors under certain conditions.

d. Taxation of Income from International Transportation

(1) Tax treaties

- (a) All treaties concluded with the countries listed below provide that profits that enterprises in one signatory nation* derive from operation of ships or aircraft in international traffic are exempt from tax in the other signatory nation:

The United States, Sweden, Denmark, Norway, Singapore, Austria, the United Kingdom, New Zealand, Malaysia, Canada, France, Germany, Brazil, Egypt, Belgium, Australia, the Netherlands, Republic of Korea,

* The countries are listed in order of their date of signature of tax treaties with Japan.

XXIV Taxation of Nonresidents and Foreign Corporations

Zambia, Switzerland, Finland, Italy, Spain, Ireland, Romania, the former Czechoslovakia, Hungary, Poland, Indonesia, China, the former U.S.S.R., Bulgaria, Luxembourg, Israel, Turkey, Viet Nam and Mexico, and South Africa.

- (b) In the case of Pakistan, only income from the operation of aircraft is exempt from tax in the other signatory nation.
 - (c) In the cases of India, Thailand, India, and Bangladesh, income from the operation of aircraft is exempt from tax in the other signatory nation, and income from the operation of ships is taxed in the other signatory nation at 50% of the normal rate.*
 - (d) In the case of Sri Lanka, income from the operation of ships or aircraft is taxed in the other signatory nation at 50% of the normal rate.
 - (e) In the case of the Philippines, income from the operation of ships or aircraft is taxed in the other signatory nation at 60% of the normal rate.
- (2) Domestic law

Japan has a special law that stipulates tax exemption to income from international transportation on a reciprocal basis. When foreign countries meet the conditions of reciprocity in accordance with the Law, enterprises based in foreign countries designated by cabinet order are exempt from certain taxes (income tax, corporation tax, inhabitants taxes and, enterprise tax) in Japan. The countries for which this exemption is granted by the cabinet order are as follows:

Country/Area	Income Source	Taxes Exempt
United States of America	Income from ocean or air transportation businesses	Income tax, corporation tax, and enterprise tax
Netherlands**	Income from ocean transportation businesses	Income tax, corporation tax, inhabitants taxes, and enterprise tax
Argentina	Income from ocean or air transportation businesses	Income tax and corporation tax
Lebanon	Income from ocean or air transportation businesses	Income tax, corporation tax, inhabitants taxes, and enterprise tax
Iran	Income from air transportation businesses	Income tax and corporation tax

* With respect to India, the rate was reduced to 25% as of 1995 and is exempt after 2000.

** Granted until the taxable year beginning 31 Dec. 2000. Granted for a period of 7 years after the convention comes into effect.

Taiwan	Income from ocean or air transportation businesses	Income tax, corporation tax, inhabitants taxes, and enterprise tax
The United Arab Emirates	Income from ocean or air transportation businesses	Income tax, corporation tax, inhabitants taxes, and enterprise tax

e. Relief from Double Taxation

There are treaties that provide relief from double taxation through foreign tax credits and Japanese residents or corporations are allowed to credit foreign taxes against their Japanese tax liability in accordance with the domestic law (see 2/5, 4. b, 3/4, 6. b and 23/4, 1. b).

In addition, Japan grants a tax sparing credit under conventions with some countries. Substantially, Japan grants a tax sparing credit by the convention between the countries listed below; Pakistan, Thailand, Malaysia,* Brazil, Sri Lanka, Zambia, the Philippines, China, Bangladesh, Viet Nam,** and Mexico.***

Under this tax sparing credit system, the amount of tax exempted or reduced under certain special incentive measures by these countries, to promote their economic development, is deemed to have been paid in these countries and thus becomes creditable with respect to Japanese taxes.

f. Inquiry and inspection rights for exchange of information

In accordance with the provisions of the relevant Tax Treaty, if supply of information is requested by the other party to the treaty, the relevant staff of the National Tax Agency, Tax Administration Bureau or taxation offices may ask questions to or conduct inspections on specified persons excluding certain cases. (Such questions and inspections may include those concerning necessary regulations such as penal codes.)

Also, tax officials can conduct a voluntary or compulsory inspection under certain conditions, to provide information necessary for the other party of the tax treaty to investigate an act of violation.

* Granted until the taxable year beginning 31 Dec. 2006.

** Granted until the taxable year beginning 31 Dec. 2010.

*** Granted until the taxable year beginning 31 Dec. 2005.

CHAPTER XXV
ORGANIZATION OF THE NATIONAL
TAX AGENCY

25/1 General

The administration of the tax system is under the general jurisdiction of the Ministry of Finance, consisting of the Minister's Secretariat, Budget Bureau, Tax Bureau, Customs and Tariff Bureau, Financial Bureau, and International Bureau. In addition to these internal bureaus, the Ministry has, as its external organization, the National Tax Agency; These bodies together constitute its external organization. The Tax Bureau of the Ministry of Finance is responsible for research and planning concerning the tax system and the drafting of tax laws, while the National Tax Agency is responsible for the enforcement of tax laws and deals with tax administration in general.

In addition, the Customs and Tariff Bureau of the Ministry of Finance is in charge of planning and formulating systems concerning tariffs, tonnage taxes, special tonnage taxes, and general custom-house administration.

[note] The Customs and Tariff Bureau consists of the Co-Ordination Division, Personnel Division, Tariff Policy and Legal Division, International Affairs and Research Division, Enforcement Division, Customs Clearance Division, and Post-Entry Examination and Customs Area Division. In addition, as regional taxation branches, eight Custom-Houses (Hakodate, Tokyo, Yokohama, Nagoya, Osaka, Kobe, Moji, and Nagasaki) and Okinawa District Custom-House are in charge of imposing and collecting tariffs, tonnage taxes, special tonnage taxes and general custom-house administration.

25/2 Tax Bureau of the Ministry of Finance (*Shuzei-kyoku*)

The Tax Bureau is mainly in charge of (1) planning and drafting taxation systems; (2) researching and planning international taxation systems, international tax treaty matters, certified public tax accountant system, and liquor business association system (including drafting relevant law and regulations); and (3) estimating tax revenues.

The Tax Bureau consists of Co-Ordination Division, Research Division, Income Tax and Property Tax Policy Division, Consumption Tax Policy Division, Corporation Tax Policy Division and International Tax Policy Division.

1. **The Co-ordination Division** is in charge of (1) formulating tax policy in general, of (2) estimating tax revenues and researching settlements of accounts and of (3) The matters related to Local Tax, Local Allocation Tax and Local Transfer Tax.
2. **The Research Division** is in charge of researching (1) domestic tax systems and (2) foreign tax systems.
3. **The Income Tax and Property Tax Policy Division** is in charge of (1) planning and drafting laws and regulations of individual income tax, inheritance tax, gift tax, land value tax, registration and license tax, and other national direct taxes, of (2) the regulations of National Taxes and collecting system and of (3) planning and drafting system of a licensed tax accountant.
4. **The Consumption Tax Policy Division** is in charge of planning and drafting laws and regulations of (1) Consumption Tax, (2) Liquor Tax and other national indirect taxes.
5. **The Corporation Tax Policy Division** is in charge of planning and drafting laws and regulations of Corporate Tax.
6. **The International Tax Policy Division** is in charge of (1) researching, planning, drafting international tax treaties and of (2) researching, planning, and drafting laws and regulations of taxation on incomes of nonresidents and foreign corporations and systems of foreign tax credit.

25/3 National Tax Agency (*Kokuzei-cho*)

1. General

The National Tax Agency, established as an external organization of the Ministry of Finance on 1 June 1949, is mainly in charge of the assessment and collection of internal taxes, which until then had been executed by the Tax Bureau.

The National Tax Agency, headed by a Commissioner, consists of the Commissioner's Secretariat and three Departments with 669 officials, several affiliated organs with 820 officials, 11 Regional Taxation Bureaus, the Okinawa Regional Taxation Office, and 524 Tax Offices with 54,696 officials (as of the end of March 2006).

2. Organization

The National Tax Agency consists of the Commissioner's Secretariat, a Taxation Department, a Revenue Management and Collection Department, and an Examination and Criminal Investigation Department. In general, the functions of the Administration are to propose plans to execute tax administration, es-

establish collective views on tax laws issue directives to Regional Taxation Bureaus, and supervise and direct Regional Taxation Bureaus and Tax Offices. The functions of each department are as follows:

a. The Commissioner's Secretariat is in charge of general affairs and coordination among departments.

It consists of five divisions and three offices: the Co-ordination Division, the Personnel Division, the Accounting Division, the Planning Division, the Information System Management Division, the Office of International Operations, the Co-ordination Office, the Office of Management Supervision, and the Office of Mutual Agreement Procedures. In addition, it has several special officers: the Health and Welfare Division, the Director (Public Relations), the Chief Internal Inspector, Director (Research and Planning), the Tax Counselor.

The office of International Operations is in charge of international taxation issues.

The Office of Management Supervision is responsible for the supervision of the administrative activities of the National Tax Agency, Regional Taxation Bureaus and Tax Offices and also evaluation of their performances. In this office, there are 40 Management Supervisors, most of whom are dispatched to Regional Taxation Bureaus.

The Director (Public Relations) promotes the awareness of taxpayers and propagates the knowledge of taxation.

The Chief Internal Inspector investigates any violation committed by officials of the Administration. There are 120 Internal Inspectors, most of whom are dispatched to Regional Taxation Bureaus.

The Director is in charge of planning concerning important matters.

The Tax Counselors handle tax consultation for taxpayers.

b. The Taxation Department consists of five divisions and two offices: the Taxation Management Division, the Individual Taxation Division, the Property Taxation Division, the Corporation Taxation Division, the Liquor Tax and Industry Division, the Consumption Tax Office, the Office of Rulings and Legal Affairs. In addition, special officers such as Director (Property Valuation) and Director (Analysis and Brewing Technology) are also assigned.

The Taxation Management Division determines basic policies of the entire Taxation Department, controls individual divisions of the Department, and coordinates office work and measures among the divisions. The Individual Taxation Division is in charge of income tax except the taxation of capital gains, withholding income tax, and consumption tax on individual proprietors. The Property Taxation Division is responsible for the inheritance tax, gift tax, land value tax, registration and license tax, securities transaction tax, property tax, and income tax on capital gains and its consumption tax. The Cor-

poration Taxation Division covers corporation tax, withholding income tax, and consumption tax on corporations. The Liquor Tax Division is in charge of the liquor tax and the administrative work of liquor. The Consumption Tax Office is in charge of indirect taxes such as the consumption tax, tobacco tax, burse tax, stamp tax, promotion of power-resource development tax, petroleum tax, liquefied petroleum gas tax, gasoline tax, etc. The Office of Rulings and Legal Affairs is in charge of: (1) supervising the application and interpretation of laws and regulations relating to imposition of income tax, corporate tax, inheritance tax, etc; (2) requests or reinvestigation regarding the taxation of the income tax, corporation tax, consumption tax, inheritance tax, etc. and; (3) matters of litigation concerning internal taxations. The Director (Property Valuation) is in charge of the valuation of properties related to the inheritance tax, gift tax, land value tax, income tax on capital gains, etc. and the Director (Analysis and Brewing Technology) is in charge of technical matters concerning liquor and other objects subject to indirect taxes.

- c. **The Revenue Management and Collection Department** consists of the Revenue Management Division and the Collection Division. The Revenue Management Division is in charge of the collection of national taxes, administration of refunds of internal tax, and business concerning Savings-for-Tax Associations. The Collection Division is in charge of the management of measures against delinquent taxes, and requests or reinvestigation and litigations thereof.
- d. **The Examination and Criminal Investigation Department** consists of the Examination Division, the Criminal Investigation Division, and the Director (International Examinations). The Examination Division directs or supervises the examination of taxation on large-scale corporations and foreign corporations. The Criminal Investigation Division investigates tax violations. The Director (International Examination) is in charge of overseas transactions (including transactions of transfer price) and affairs relating to foreign corporations among office work of the Examination Division. Officials of this Department are authorized to examine or investigate taxpayers directly, as an examiner or investigator.

3. Affiliated Organs

The National Tax College, National Tax Tribunal, , and National Tax Council, are the affiliated organs of National Tax Agency. National Tax Council has no permanent administrative organization. Their functions are as follows:

- a. **The National Tax College** mainly offers training courses for Ministry of Finance officials to engage in NTA administrative work.

In addition to the central institute, 12 regional training centers are set up in cities where Regional Taxation Bureaus and Okinawa Regional Taxation Office are located.

The central institute offers basic training for university graduates (4 months), Advanced Course I for high school graduates (1 year), Advanced Course II for university graduates (7 months), a Research Course (15 months), an International Tax Seminar (2 months for the Basic Course and 4 months for the Advanced Course), and Short-Term Training, etc.

The 12 regional training centers offer short-term training courses and correspondence courses, and in addition to these at Kanto-Shinetsu Tokyo, Nagoya, and Osaka offer the Primary Course for high school graduates (12 months) and the basic training course (3 months) for new employees.

- b. The National Tax Tribunal** is an institution that makes decisions on requests for reconsideration with respect to dispositions made in accordance with the laws concerning national taxes. It was established in May 1970 in order to protect the legitimate rights and interests of taxpayers through appropriate and prompt decisions and contribute to appropriate operation of tax administration.

The National Tax Tribunal has its Head Office in Tokyo, plus Regional Tax Tribunals in twelve major cities and Branch Offices in seven major cities.

The Tribunal consists of a President, Vice-president, 177 Commissioners, 87 Deputy Commissioners, 174 or fewer Tax Tribunal Examiners, and Administration Officers. Commissioners are responsible for investigation and examination of the cases of reconsideration requests made to the President of the National Tax Tribunal, and Deputy Commissioners carry out administrative work for Commissioners under instructions from Commissioners.

- c. The National Tax Council** is a consolidation of the National Tax Council, Board of Review of Certified Public Tax Accountants, and Central Council on Liquor, following the reorganization of the ministries and agencies enforced in January 2001. Under the Council, the National Tax Council Subcommittee, Tax Accountant Subcommittee, and Liquor Subcommittee were formed.

- (1) The National Tax Council Subcommittee investigates and discusses matters on which the Commissioner of the NTA requires it to present an opinion. Such matters include a case where an interpretation of laws and regulations of the Commissioner of the National Tax Tribunal is different from the view indicated in a notice issued by the Commissioner of the NTA.
- (2) The Tax Accountant Subcommittee conducts tax accountant examinations and deliberates on disciplinary actions taken to tax accountants upon the inquiry of the Minister of Finance.
- (3) The Liquor Subcommittee examines establishing labeling standards of

liquors, etc..

25/4 Regional Taxation Bureaus(Kokuzei-kyoku)

Regional Taxation Bureaus are responsible for the assessment and collection of national taxes within their jurisdiction. Each Bureau directs and supervises, under the superintendence of the National Tax Agency, Tax Offices situated in its jurisdiction. In addition, the Bureau directly handles the assessment and collection of taxes for certain taxpayers.

In general, the Regional Taxation Bureau is composed of five departments: a Management and Co-ordination Department; the First Taxation Department, the Second Taxation Department, the Revenue Management and Collection Department and; the Examination and Criminal Investigation Department. (In Kanazawa, Takamatsu, and Kumamoto Regional Taxation Bureaus, the First Taxation Department and the Second Taxation Department are unified into the Taxation Department). Their activities are in general similar to those of the National Tax Administration.

1. **The Management and Co-ordination Department** is generally composed of the following divisions: the Co-ordination Division, the First Personnel Division, the Second Personnel Division, the Accounting Division, the Planning Division, the Health and Welfare Division, the Information System Management Division, the Tax Counsel Office, the Office of Public Relations, and the Director (Building and Repairs). In addition, some Regional Taxation Bureaus have other special officers: the Director (Information System Management), the Special Office (Tax Accountant Supervision), and the Special Officer (Personnel).
2. **The First Taxation Department** is generally composed of the Taxation Management Division, the Individual Taxation Division, the Property Taxation Division, the Information and Examination Division, the Office of Litigation (or Litigation Officer), and the Director (Property Valuation). The number of Information and Examination Divisions varies with each Bureau. (For example, the Tokyo Regional Taxation Bureau has four Information and Examination Divisions, the Osaka Regional Taxation Bureaus have three Divisions, and the Kanto-Shinetsu and Nagoya Regional Taxation Bureau has two Divisions, respectively.) In addition, some Regional Taxation Bureaus may have the Special Office (Planning and Co-ordination) Chief, Examiner.
3. **The Second Taxation Department** is generally composed of the Corporation Taxation Division, the Consumption Tax Division, the Information and Examination Division, the Liquor Tax Division, the Office of Analysis and Brewing Technology, and the Special Officer (Liquor Tax Industry). The

number of Information and Examination Divisions varies with each Bureau. (For example, the Tokyo Regional Taxation Bureau has three Information and Examination Divisions, and Kanto-Shinetsu, Nagoya, and Osaka Regional Taxation Bureaus have two Divisions, respectively.) In addition, some Regional Taxation Bureaus may have the Chief Examiner. The Office of Analysis and Brewing Technology is in charge of analyzing and appraising liquor, materials subject to indirect national tax and instructions on brewery.

4. **The Revenue Management and Collection Department** is generally composed of the Revenue Management Division, the Collection Division, the Office of Litigation (or Litigation Officer), and Chief Revenue Officers. Special Revenue Officers are stationed at the Sapporo, Sendai, Kanto-Shinetsu, Tokyo, Nagoya, Osaka, Hiroshima, and Fukuoka Regional Taxation Bureaus. At each Bureau, Revenue Officers are in charge of procedure for collection of large-valued tax delinquencies and other difficult matters under management of 41 Chief Revenue Officers and 21 Special Revenue Officers. In addition, some Regional Taxation Bureaus may have the Task Force Divisions, the Special Collection Co-ordination Divisions, and Directors (Postponement of Tax Payment and Tax Payment in Kind).
5. **The Examination and Criminal Investigation Department** is generally composed if the Management Division (Examination), the Special Examiners, the Chief Examiners, the Management Division (Criminal Investigation), the Special Investigators, and the Chief Investigators. Chief Examiners are responsible for the examination of: (1) corporation tax and consumption tax for domestic corporations (with capital of ¥100 million or more) and foreign corporations; (2) consumption tax on Government and Corporations concerned with the Public Interest, etc. and; (3) the tax base of taxpayers specifically designated by the Regional Commissioner. Examinations are carried out by Examiners under the management of the Chief Examiners and the Special Examiners. The Special Examiners are in charge of the examination of particularly large corporations.

Criminal Investigations are carried out by Investigators under the management of the Chief Investigators and the Special Investigators. The Special Investigators are mainly in charge of collecting information related to the district and of seeking cases for investigation.

The organization of the Examination and Criminal Investigation Departments of the Tokyo, Nagoya, and Osaka Regional Taxation Bureaus are somewhat different from the above description, mainly because they are divided into the Examination Departments and the Criminal Investigation Department. In other words, the Tokyo Regional Taxation Bureau has four Examination Departments and one Criminal Investigation Department; the Na-

goya Regional Taxation Bureau has one Examination Department and one Criminal Investigation Department; and the Osaka Regional Taxation Bureau has two Examination Departments and one Criminal Investigation Department.

25/5 Tax Office (Zeimusho)

The Tax Office is responsible for the assessment and collection of national taxes under the direction and supervision of the Regional Taxation Bureaus. Every tax office deals with all types of national taxes. In other words, there is no tax office only in charge of specific taxes such as the case those in charge of excise taxes in some countries. The Tax Office is the organ most closely connected to taxpayers.

Tax offices are located in principal cities all over the country. The organization of tax offices varies according to their scale. Ordinarily, they are composed of one division and three groups under the District Director of the Tax Office, namely, one administrative division (a Co-ordination Division), and three groups (the Revenue Management and Collection Group, the Individuals Examination Group, and the Corporations Examination Group). In addition, some tax offices have special officers: the Special Officer (Public Relations) and the Chief Examiner (Liquor Tax and Industry). In the tax office, each official is in charge of respective assignments such as internal work, examination, and general guidance.

Standard Organization of Tax Offices (*Zeimusho*)

Name of Division	Main Duties
Co-ordination Division	Personnel, accounting, welfare, and overall office co-ordination
Revenue Management and Collection Group	Collection of internal taxes, refund of internal taxes, and affairs concerning Savings-for-Tax Associations
Individuals Examination Group	Assessment of income tax (except withholding income tax at the source or income tax on capital gain), consumption tax relating to individual proprietor's transfer of assets.
Assets Examination Group	Assessment of inheritance tax, gift tax, and income tax on capital gain.
Corporations Examination Group	Assessment of corporation tax, withholding income tax at the source, consumption tax relating to corporation's transfer of assets, etc., other national indirect taxes, and liquor tax.

Note: Most tax offices are organized according to this standard structure. In the case of relatively small tax offices, there are some simplifications of this organization; for example, the Examination Group (Individuals) and Examination Group (Corporations) are unified into a single Examination Group.

Appendix I Trends in Tax

Tax reform, etc.	Background (socioeconomic conditions, etc.)	Taxation on individual incomes
A. Drastic tax reform (December 1988, etc.)	<ul style="list-style-type: none"> • Increasing incomes and their leveling • Diversified consumptions and intensified consumption of services • Aging population • Globalization of economic transactions 	<ul style="list-style-type: none"> • Mitigation of progressive tax rate structure • Rising the tax threshold
B. Land taxes reform, etc. (FY1991, etc.)	<ul style="list-style-type: none"> • Expanding gaps in assts due to soaring land prices • Enacting the Basic Land Act (Basic idea to maintain the publicity of land) 	
C. Tax reform (November 1994, etc.)	<ul style="list-style-type: none"> • Accelerating of aging population • Increasing incomes and their leveling • Collapse of the bubble economy and faltering economy 	<ul style="list-style-type: none"> • Temporary tax reduction • Legislating permanent tax reduction (enforced in 1995) (Progressive lifting the tax threshold) <div style="border: 1px dashed black; padding: 5px; margin-top: 10px;"> <ul style="list-style-type: none"> +Special tax reduction (1995) +Special tax reduction (1996) </div>
D. Corporate taxes reform, etc. (FY 1998, etc.)	<ul style="list-style-type: none"> • Economic structure reform • Severe economic conditions 	<ul style="list-style-type: none"> • Special tax reduction (for the current and addition portions)
E. Permanent tax reduction, etc. (FY 1999, etc.)	<ul style="list-style-type: none"> • Severe economic conditions 	<ul style="list-style-type: none"> • Lowering the maximum tax rate (65% → 50%) • Tax reduction at a fixed-rate

Reform, etc. in Recent Years

Taxation on corporations	Taxation on consumption	Taxation on assets, etc.
<ul style="list-style-type: none"> Lowering the basic tax rates, etc. (42% → 40% on April 1, 1989; 40% → 37.5% on April 1, 1990) 	<ul style="list-style-type: none"> Introducing consumption tax Streamlining the individual indirect taxes 	<ul style="list-style-type: none"> Reducing inheritance tax (Mitigation of progressive tax rate structure Increase basic exemptions, etc.) Re-examining interest taxation Taxation, in principle, at capital gains from stock transfers
	<ul style="list-style-type: none"> Re-examining the consumption tax system (Expanding non-taxable areas, reducing special measures for small and medium enterprises, etc.) 	<ul style="list-style-type: none"> Making appropriate taxation at capital gains from land transfer Introducing land value tax (enforced in 1992)
	<ul style="list-style-type: none"> Legislating of rising the consumption tax rate (enforced in FY 1997) Raising the consumption tax rate (3% → 4%) Reducing special measures for small and medium enterprises, etc. Introducing local consumption tax (1%) (enforced in FY 1997) 	<ul style="list-style-type: none"> Reducing inheritance tax (Mitigation of progressive tax rate structure Increase in basic exemptions, etc.)
<ul style="list-style-type: none"> Lowering the basic tax rates (Corporate tax: 37.5% → 34.5%) (Corporate business tax: 12% → 11%) Making the taxation basis appropriate 		<ul style="list-style-type: none"> Suspending land value taxation Relieving taxation at capital gains from land transfer
<ul style="list-style-type: none"> Lowering the basic tax rates (Corporate tax: 34.5% → 30%) (Corporate business tax: 11% → 9.6%) 	<ul style="list-style-type: none"> Limiting the use of consumption tax (for the portion of central government) to social welfare 	<ul style="list-style-type: none"> Abolition of securities transaction tax and bourse

Appendix I Trends in Tax

Tax reform, etc.	Background (socioeconomic conditions, etc.)	Taxation on individual incomes
F. FY2003 tax reform	<ul style="list-style-type: none"> • Overhauling the present tax system forward a construction of a desirable tax system 	<ul style="list-style-type: none"> • Abolition of the special deduction for spouses (exceeding the amount of the deduction for spouses) (applicable from FY2004 for income tax assessment and from FY2005 for individual inhabitant tax assessment)

Reform, etc. in Recent Years (Continued)

Taxation on corporations	Taxation on consumption	Taxation on assets, etc.
<ul style="list-style-type: none"> • R&D tax credit and IT investment incentives to improve the competitiveness of Japanese industry 	<ul style="list-style-type: none"> • Reducing the tax exempt threshold for small and medium-size corporations, etc. (applicable from FY2004) 	<ul style="list-style-type: none"> • Reduction of inheritance tax including reviewing the tax rate structure and a reduction of the top marginal tax rate (70%→50%) • Introduction of the taxation system for settlement at the time of inheritance

Appendix I-1

A Points of the Drastic Tax Reform (December 1988, etc.)

1. Reduction and rationalization of income tax burdens

- (1) Mitigation of the progressive tax rate structure
 - ① Income Tax: 10.5%~60% in 12 brackets → 10%~50% in 5 brackets
 - ② Individual Inhabitants Tax:
5%~16% in 7 brackets → 5%~15% in 3 brackets
- (2) Increase in standard personal exemptions
 - ① Increase in the basic exemption, the exemption for spouses, and the exemption for dependents (¥330,000 → ¥350,000)
 - ② Application of the special exemption of ¥450,000 for dependents ages 16 to 22 instead of the ordinary exemption of ¥350,000
 - ③ Increase in the special exemption for spouses (¥165,000 → ¥350,000), and increase in the annual maximum eligible income (¥8 million → ¥10 million)
- (3) Others
 - ① Increase in various special personal exemptions, including additional exemptions for severely handicapped individuals living with the taxpayer.
 - ② Increase in exemptions for family employees of business proprietors filing white returns
(for spouses: ¥600,000 → ¥800,000, for others: ¥450,000 → ¥470,000)
Note: Similar reforms for Individual Enterprise Tax
 - ③ Increase in the retirement income deduction
(30years of employment: ¥10 million → ¥15 million)
 - ④ Guarantee of minimum business expenses for those engaged in domestic work
 - ⑤ Abolition of the aggregation of household members' income from assets, etc.

2. Measures for more equitable distribution of tax burdens

- (1) Taxation on capital gains from securities transactions
 - ① Income Tax: separate taxation at 20% through the filing of final returns or, at the taxpayer's choice, separate taxation withheld at the source, at 20% of the deemed gain of 5% of the proceeds from the sale of listed stocks and other publicly traded securities (Not applicable to proceeds from stocks acquired before initial public offering (IPO) and sold within one year of IPO)
 - ② Individual Inhabitants Tax: separate taxation at 6% except where separate

taxation at source is chosen for Income Tax

- (2) Repeal of the estimated expenses system for medical fees paid by social insurance plans to doctors whose receipts exceed ¥50 million
- (3) Limitation of the deductibility of interest payments on funds borrowed for land acquisition (no deduction for the first four years after acquisition)

3. Reduction of the inheritance tax

- (1) Increase in the minimum taxable threshold
(¥20 million + [¥4 million × the number of statutory heirs]
→ ¥40 million + [¥8 million × the number of statutory heirs])
- (2) Widening of tax brackets and reduction of the maximum rate
(75% → 70%)
- (3) Enhanced measures to reduce the inheritance tax burden for surviving spouses
(tax exempted inheritance: 1/2 of total inheritance
→ the amount of legal inheritance,
minimum guaranteed inheritance: ¥40 million → ¥80 million)
- (4) Increase in tax credits for the handicapped and others individuals
- (5) Enhancement of the special inheritance tax provision for small-lot land and other land
(land for business use [40% → 60%], land for residential use [30% → 50%])
- (6) Measures to counter tax evasion
 - ① Limitation of the number of adopted children who may be included as statutory heirs for inheritance tax calculation
 - ② Calculation of the tax on inherited real estate based on its purchase price if the land is purchased during the last three years of life
- (7) Corresponding change in the gift tax
(widening of tax brackets, reduction of the maximum tax rate (75% → 70%), and increase in the exemption for spouses)
- (8) Application date
(except (6), for inheritances or gifts made on or after 1 January 1988 and, regarding (6) above, those made on and after the date the law came into effect)

4. Fundamental reform of indirect taxes

- (1) Introduction of Consumption tax
Introduction of a consumption tax that is levied lightly and broadly
[Goals]
 - To facilitate the shifting of the tax burden and to prevent excessive price

increases

- To reduce and rationalize compliance costs of small and medium-sized enterprises

[Basic Structure]

- Taxation at each stage of sale and provision of goods and services by business entities
- Credit for tax paid to suppliers with respect to the tax on the enterprise's sales, in order to avoid double taxation

Crediting based on accounting records or documents such as statements of delivery, bills, etc.

Calculation of tax credit either by the itemization method or the proportional method when the value of tax-exempt sales exceeds 5% of total sales

- Tax-exempt transactions
 - Exports
 - Other tax-exempt transactions

Sale or lease of land, sale of securities and means of payment, interest on loans/insurance premiums, postage, other stamps and similar items, certification fees for resident and family registration, international postal money orders/international postal money transfers/foreign exchange transactions, medical services given under medical insurance laws, some types of social welfare services/nursery schools/maternity homes, and tuition and entrance examination fees for schools

- Tax rate: 3% (6% on passenger automobiles for the first 3 years except those 500 cc or below)
- Self-assessment and payment twice a year (if the tax period is one calendar year or one fiscal year, and there is an interim return and payment), or once a year for small-sum taxpayers
- Introduction of a simplified method for mitigating tax compliance costs of small and medium-sized business entities with annual sales lower than ¥500 million that are allowed to calculate their tax based only on the sales amount using the deemed rate of purchases: 90% for wholesalers and 80% for others
- Exemption for small enterprises (with annual sales below ¥30 million)

Introduction of a marginal exemption, by which a part or all of the tax payment is exempted, to narrow the gap between taxable and tax-exempt enterprises (for enterprises with annual sales below ¥60 million)
- Existing indirect taxes to be abolished

National taxes: Commodity tax, playing-cards tax, sugar excise tax, admission tax, and travel tax

Local taxes: Electricity tax, gas tax, and timber delivery tax
- Effective date 1 April 1989

- Transitional measures: necessary measures to be taken concerning construction contracts signed before the official announcement of the law, advanced payment of transportation, admittance, and other fees

The Consumption Tax is administered by the National Tax Agency which also administers corporate income tax.

- (2) Revision of existing indirect taxes
 - ① Liquor tax
 - Abolition of ad valorem liquor taxes and the grading system
 - Reassessment of tax rates on various liquor in light of the reductions in tax rate differentials between categories
 - Reduction of tax rates in consideration of the increased burden from the new consumption tax
 - ② Tobacco excise tax
 - Renaming of the “Tobacco tax” and unification of taxation methods for specific duty systems while maintaining the current tax burden
 - Reduction of tax rates in consideration of the increased burden from the new consumption tax
 - ③ Others
 - Stamp tax: exclusion of five document types from those taxable
 - Securities transaction tax: reduction of the tax rate on stocks, etc.
 - Bourse tax: reassessment of tax rates to balance taxes on commodities and securities
 - Petroleum tax: adoption of a specific duty system while maintaining the current tax burden

5. Reduction of corporation tax

- (1) Reduction of the corporation tax rate

Ordinary corporations	(42% → 40% [1989] → 37.5% [1990])
Small and medium-sized corporations	(30% → 29% [1989] → 28% [1990])
Corporations in the public interest, cooperatives, associations, etc.	(current rate of 27% unchanged)

Note: On cooperatives with membership over 500,000 and annual sales over ¥100 billion (which serve only a specific area or region), 30% on the portion of income over ¥1 billion after 1989

 - Abolition of the reduced rate on income distributed as dividends

	(32% → 35% [1989] → 37.5% [1990])
--	------------------------------------
- (2) Reduction of the portion of dividends received excluded those from taxable income

	(100% → 90% [1989] → 80% [1990])
--	-----------------------------------
- (3) Increase in the maximum value of small-sum depreciable assets that may be

included with expenses in the year of purchase

(less than ¥100,000 → less than ¥200,000)

- (4) Reassessment of the foreign tax credit system

6. Distribution of Consumption tax revenue to local governments

- (1) Introduction of the Consumption Transfer tax
 - Transfer of 1/5 of Consumption Tax revenue to local governments
 - Transfer of 6/11 of Consumption Transfer Tax revenue to prefectural governments and 5/11 to municipal governments
- (2) Additional tax items that are subject to the Local Grant Tax
 - Addition of Consumption Tax to the items that are subject to Local Grant Tax and granting of 24% of Consumption Tax revenue (except for the portion from the Consumption Transfer Tax) to local governments through the Local Grant Tax

Appendix I-2

B Points of the Land Taxes Reform, etc. (FY1991, etc.)

I Re-examining the Land Taxation System

1. Introduction of land value tax

Land value tax will be introduced in the following details:

(1) Objects of taxation

Domestic land and lease rights, etc. owned by individuals and corporations (hereafter referred to as “land, etc.”).

(2) Taxpayers

Individuals and corporations who own land, etc. as of January 1 every year (hereafter referred to as the “taxation period”).

(3) Evaluation

Land, etc. shall be evaluated at the market value during the taxation period.

Note: The market value is based on the appraisal value of inheritance tax.

(4) No taxation

Nontaxable land, etc. shall be:

1. Land, etc. owned by public corporations, including the government and local public entities, that are listed in Schedule 1 of the Corporation Tax Law
2. Land, etc. owned by corporations in public interest listed in Schedule 2 of the Corporation Tax Law (excluding the land, etc. used for businesses other than those stipulated in the articles of incorporation, etc. and the land, etc. with no utilization plan for the businesses stipulated in the articles of incorporation, etc.)
3. Land, etc. which is provided for any of the following public interests and which is stipulated in Schedule I
 - a. Land, etc. relating to the preservation of nature, land, etc.
 - b. Land, etc. relating to medicine, social welfare, etc.
 - c. Land, etc. relating to culture, education, etc.
 - d. Land, etc. relating to traffic, telecommunications, etc.
 - e. Land, etc. relating to city water, energy, etc.
 - f. Other land, etc.
4. Land, etc. provided for dwelling with the following conditions (the taxable area (applicable to floor space per condominium) is limited to 1,000 m², if the area is beyond 1,000 m²)
 - a. Dwelling house owned and dwelled by the person (limited to one)
 - b. Dwelling houses leased to others (excluding director’s dwelling houses)

owned by the company)

5. Land, etc. whose value per m^2 is ¥30,000 or below with no lease right (hereafter referred to as “Site Value”)

(5) Tax base

1. A total of values of land, etc. owned during the taxation period (hereafter referred to as the “tax value”).
2. A special measure shall be taken to reduce the value included in the tax value into one-fifth of the value of land, etc. for residential sites planned for sale by a certain bodies that operate business making residential sites or housing business that sells good residential sites or houses.
3. A special measure shall be taken to reduce the value included in the tax value into one-second of the value of the land, etc. for the land, etc. listed in Schedule II.

(6) Basic exemptions and taxable amount

1. The taxable amount is the remaining sum where basic exemptions are deducted from tax value.
2. The sum of basic exemptions shall be either of the following cases, which ever is larger.
 - a. ¥1 billion (for individuals, corporations with a capital or investment of ¥100 million or less, corporations with no capital and investment (excluding mutual corporations, etc. under the Insurance Business Law); ¥1.5 billion for cooperatives, etc. listed in Schedule III of the Corporation Tax Law and for corporations in public interest, etc. listed Schedule II of the Corporation Tax Law)
 - b. For site value whose value per m^2 is beyond ¥30,000, the sum obtained by multiplying the space of the land, etc. by ¥30,000 (for the land, etc. where a lease right is established, the sum obtained by multiplying the ratio of the lease right, etc. by ¥30,000; for land, etc. subject to the special measure for tax value, the sum obtained by multiplying ¥30,000 by the reduction ratio concerned (for the said land, etc. where a lease right, etc. is established, the sum obtained by multiplying the reduction ratio concerned by the ratio of the lease right))

(7) Tax rate

0.3%. However, the rate is 0.2% for 1992.

(8) Return and payment

The taxpayer shall file return from October 1 to October 31 every year and make installment payments of tax on the day or by March 31 of the following year. However, the taxpayer shall file return from November 16 to December 15 and make installment payments of tax on the day or by March 31 of the following year for 1992.

- (9) Place to pay tax, etc.
1. A provisions for the place to pay tax, examination and investigation right, and requesting governmental and public offices for cooperation shall be formulated in accordance with income tax and corporate tax.
 2. A provision shall be formulated so that the mayor provides tax officials with opportunities to check property tax ledgers upon request from the district director of the tax office, etc.
 3. Other necessary provisions shall be formulated tax.
- (10) Applicable period, etc.
1. Land value tax shall be applied from the taxation period for 1992.
 2. Conditions of the burden of land value tax shall be examined at least every five years by considering for appropriate assessment of property tax and conditions of the entire tax burden on landowners. In addition, when necessary, the National Tax Agency shall take appropriate measures for taxable objects and tax rates, etc.

2. Taxation on capital gains

- (1) Taxation Method for capital gains from the transfer of land, etc.
1. Taxation on capital gains from land, etc. owned by individuals
 - a. Rate of long-term capital gains shall be raised as follows:

Capital gains after special exemption	Current	After the reform
Portion of ¥40 million or less	20%	30% without variation
Portion above ¥40 million	25%	

Note: The above revision shall be applied to long-term capital gains from land transfer on and after January 1, 1992.
 - b. The applicable period shall be extended for another five years (1) for the special measure distinguish long-term capital gains and short-term capital gains by holding period of five years and (2) for the special measure where the period of holding land, etc. subject to the special taxation measure on business income, etc. relating to land transfer is set to five years or less.
 - c. The applicable period shall be extended for another five years for the special measure on business income, etc. relating to transfer of land owned for an extremely short period
 2. Taxation on capital gains from land, etc. owned by a corporation
 - a. For capital gains from land, etc. (excluding inventories relating to continuous business selling houses and developed residential lots), a special measure shall be taken to impose an additional tax of 10% in addition to

ordinary corporate tax.

However, capital gains from land, etc. subject to the capital gains taxation system relating to land, etc. owned for a short period or for an extremely short period shall be excluded.

- b.** The applicable period shall be extended for another five years for the special measure where a period of holding land, etc. subject to the capital gains taxation system relating to land, etc. owned for a short period is set to five years or less.
- c.** The applicable period shall be extended for another five years for the capital gains taxation system relating to land, etc. owned for an extremely short period, in addition to changing the current system of imposing additional tax of 30% to the separate taxation system where 30% tax rate is added to the ordinary corporate tax rate.

Note: The above revision shall be applied to the transfer of land, etc. on and after January 1, 1992.

(2) Special measure for reduction tax rate relating to long-term capital gains obtained by an individual

- 1. In addition to the measures stated below, the applicable period shall be extended for another five years for the special measure for taxation at long-term capital gains in case land, etc. is transferred in order to develop good residential lots.
 - a.** Lowering the tax rate to 15% (from current 20%)
 - b.** Re-examining for the expansion of applicable objects, etc.
- 2. Concerning the special measure for taxation on long-term capital gains from transfer of dwelling assets, capital gains after special exemptions, where 10% tax rate is applied, shall be expanded to ¥60 million (currently ¥40 million).

Note: The above revision shall be applied to long-term capital gains from land transfer on and after January 1, 1992.

(3) Special measure for taxation on long-term capital gains from transfer of particular farmland in urbanization promotion areas is abolished after a necessary transitional measure shall be taken.

Note: The transitional measure shall be effective until May 31, 1993. A long-term capital gain from the transfer on and after January 1, 1992, is imposed at 27.5% uniformly. In addition, other measures shall be taken for special exemptions and special measure for replacement of land by purchase.

3. Revision of inheritance tax

- (1) Concerning farmland in urbanization promotion areas of specified cities in the three major metropolitan areas, the special measure deferring inheritance tax payment shall be abolished after a necessary transitional measure is introduced.

However, for farmland, the diversion of which has been more restricted due to a revision of the Production Green Space Law, that is used for agriculture in green space for production, the special measure shall be applied continuously (in this case, tax exemption for engaging agriculture for 20 years and more shall not be applied.)

- (2) For assessment of land for inheritance tax, the point of time to assessment shall be adjusted to that of the posted land value (January 1, every year) from assessment for 1992, and the assessment ratio shall be raised for fairness and balance.

II. Re-Examining Consumption Tax

1. Expanding nontaxable objects

The following transfers of assets shall be nontaxable.

- (1) Providing service relating to accouchement
- (2) Providing services of burial and cremation stipulated in Article 2 of the Burial Grounds, Burials, etc. Law.
- (3) Transfer, lease, repair, and contracted manufacture of articles for a certain degree of the handicapped
- (4) Transfer, etc. of assets, which is conducted as a class II social welfare service stipulated in the Social Welfare Service Law
- (5) Providing home care services in accordance with the Old-Age Persons' Welfare Law
- (6) Providing services for the following charges relating to education stipulated in Schedule 1-18 of the Consumption Tax Law
 1. Admission fees
 2. Facility charges
 3. Charges for issuing student registration certificates
- (7) Transfer of textbooks (certified textbooks) stipulated in School Education Law
- (8) Leasing dwelling houses (excluding temporary leases of dwelling houses)

2. Changes of Special Measures for Small and Medium Enterprises

The upper limit of taxable sales for the simplified taxation system shall be ¥400 million (currently ¥50 million).

Deemed rates of purchases shall be classified into four classes, namely 90%, 80%, 70%, and 60% (currently two classes).

The upper limit that the marginal exemption system is applicable shall be ¥50 million (currently ¥60 million).

Appendix I-3

C Points of Tax Reform (November 1994, etc.)

From the standpoint of realizing a welfare state embodying fairness and dynamism, the government decreased the tax burden by changing the tax structure of individual income tax by relaxing progressiveness in order to alleviate the sentiments of a progressive tax burden, especially among the middle income class. At the same time, the government increased the weight of the consumption tax in the tax system by increasing the consumption tax rate and by fundamental reform of the special rules applied to small businesses, in order that the burden will be shared broadly by all members of society, which is necessary to maintain stable fiscal programs. The details of tax reform are as follows:

I. The tax burden for individual income tax and individual inhabitant tax was decreased.

1. Reformation of Tax Rate Structures

(1) Individual Income Tax

The tax rates changed as follows:

Before the reform		After the reform	
Taxable Income (million)	Tax Rate	Taxable Income (million)	Tax Rate
over ¥0up to ¥3	10%	over ¥0up to ¥3.3	10%
over ¥3up to ¥6	20%	over ¥3.3up to ¥9	20%
over ¥6up to ¥10	30%	over ¥9up to ¥18	30%
over ¥10up to ¥20	40%	over ¥18up to ¥30	40%
over ¥20	50%	over ¥30	50%

(2) Individual Inhabitants Tax (local tax)

Tax rates will be changed as follows:

Before the reform		After the reform	
Taxable Income (million)	Tax Rate	Taxable Income (million)	Tax Rate
over ¥0up to ¥1.6	5%	over ¥0up to ¥2.0	5%
over ¥1.6up to ¥5.5	10%	over ¥2.0up to ¥7.0	10%
over ¥5.5	15%	over ¥7.0	15%

2. Basic Exemptions

The amount of the basic exemption, exemption for spouses, special exemption for spouses, and exemption for dependents was increased.

(1) Individual Income Tax Exemption

	Before the reform	After the reform
Basic Exemption	¥350,000	¥380,000
Exemption for Spouses	¥350,000	¥380,000
Special Exemption for Spouses	¥350,000	¥380,000
Exemption for Dependents	¥350,000	¥380,000

(2) Individual Inhabitants Tax (local tax)

	Before the reform	After the reform
Basic Exemption	¥310,000	¥330,000
Exemption for Spouses	¥310,000	¥330,000
Special Exemption for Spouses	¥310,000	¥330,000
Exemption for Dependents	¥310,000	¥330,000

3. Deduction for Employment Income

As for individual income tax, the income bracket for employment income deduction no less than 20% was broadened.

Deduction Rate	Before the reform	After the reform
40%	Income no more than ¥1,650,000	Income no more than ¥1,800,000
30%	¥3,300,000	¥3,600,000
20%	¥6,000,000	¥6,600,000

4. Reducing Burdens of Inheritance Tax

1. Broadening inheritance tax bracket

The inheritance tax rates shall be revised as follows:

Tax rate	Current	After the reform
10%	¥ 7 million or less	¥ 8 million or less
15%	¥ 14 million or less	¥ 16 million or less
20%	¥ 25 million or less	¥ 30 million or less
25%	¥ 40 million or less	¥ 50 million or less
30%	¥ 65 million or less	¥100 million or less
35%	¥100 million or less	
40%	¥150 million or less	¥200 million or less

45%	¥200 million or less	
50%	¥270 million or less	¥400 million or less
55%	¥350 million or less	
60%	¥450 million or less	¥ 2 billion or less
65%	¥ 1 billion or less	
70%	over ¥1 billion	over ¥2 billion

2. Raising the inheritance tax threshold

The fixed amount exemption and the proportional exemption for heir at law shall be raised as follows:

	Current	After the reform
Fixed amount exemption	48 million	50 million
Proportional exemption for heir at law	Sum obtained by multiplying ¥9.5 million by the number of heir at law	Sum obtained by multiplying ¥10 million by the number of heir at law

3. Expanding measures for relieving inheritance tax burdens on the spouse

The minimum guarantee for relieving burdens on the spouse shall be raised as follows:

Current

¥80 million

After the reform

The objects of tax relief shall not include assets masqueraded or hidden.

5. Temporary Tax Reduction

Considering current conditions in the Japanese economy, a temporary tax reduction of 15% (a maximum amount of ¥50,000) was implemented for individual income tax and 15% (a maximum amount of ¥20,000) was implemented for inhabitants tax for 1995.

II. Reformation of Consumption Tax

The consumption tax was changed. Considering economic conditions, the following amendments became effective as of 1 April 1997

1. Increasing the Tax Rate

The tax rate of the consumption tax was stipulated to increase from 3% to 4%.
(Note)

The tax rate of the “local consumption tax,” newly established which is explained later in this Appendix, is 25% on the amount of consumption tax (equal to 1% consumption tax). Therefore, the combined rate of both the

consumption tax and “local consumption tax” is 5%.

2. Special Rules for Small Businesses

(1) Limiting Tax Exemptions for Small Businesses

A newly instituted corporation with capital of more than ¥10 million was no longer allowed to enjoy a business exemption in the first two years.

(2) Simplified Taxation System

The limit of the taxable sales for businesses that can claim through the simplified taxation system was reduced from ¥400 million to ¥200 million.

(3) Marginal Deduction System

The marginal deduction system was abolished.

3. Tax Credit for Consumption Tax on Purchases

Under the new system, taxpayers who claim tax credit on purchases must keep a bill, receipt, statement of delivery, or other invoice that shows the real transaction, in addition to bookkeeping records.

4. Re-examination clause

As for the level of the consumption tax and local consumption tax rate, the government, if necessary, was to take necessary action by 30 September 1996 (6 months before the enforcement of the revised consumption tax system), with due consideration of the financial source for fiscal needs, such as social welfare, the degree of progress of administrative and financial reforms, the proper review of special tax measures and the consumption tax system, and the fiscal situation (see Appendix IV).

III. Increasing Local Tax Revenue

“Local consumption tax” was to be introduced, as a prefectural tax, in place of the consumption transfer tax. The rate of the local consumption tax was fixed at 25% of the consumption tax (equivalent to consumption tax rate of 1%). The implementation of the local consumption tax was entrusted to the national government in order to alleviate the taxpayers’ burden to comply with administrative formalities.

Appendix I-4

Confirmation of the Consumption Tax Rate (25 June 1996)

The Japanese government provided final confirmation at the Cabinet meeting on 25 June 1996, for its decision to raise the consumption tax rate from 3 percent to 5 per cent on 1 April 1997, as stipulated in the Tax Reform Act of 1994.

The government's Tax Commission re-examined whether the stipulated consumption tax rate is appropriate in light of the review clause in the Tax Reform Act and concluded that the rate of 5 per cent does not need to be changed.

(NOTE1) Review Clause

The Tax Reform Act of 1994 stipulates that the government, if necessary, should, by the end of this September, take any appropriate measures it deems necessary regarding the consumption tax rate, with due consideration of the following items: (1) the costs of social security; (2) progress in administrative and fiscal reforms; (3) the proper review of taxation and; (5) the fiscal situation in general.

(NOTE2) Outline of the Tax Reform Act of 1994

The Tax Reform Act passed through the Diet on 25 November 1994, intended for the reform of the tax structure in light of an aging society.

With this reform, income tax is cut while consumption tax is increased so that the burden created by an aging society should be shared by all members of society. (Decreasing the burden of the income tax and local inhabitants tax)

As for the income tax and local inhabitants tax, the tax rate structure has been leveled and the tax threshold has been raised since 1995.

This permanent tax cut amounts to ¥3.5 trillion per annum, which corresponds to the revenues to be generated by the increase in the consumption tax.

In addition, a temporary tax reduction of ¥2 trillion was implemented in 1995 and 1996 in order to stimulate private consumption.

Consequently, a ¥16.5 trillion tax reduction has been realized for the three years prior to the increase in the consumption tax.

※ A temporary tax reduction of ¥5.5 trillion was implemented in 1994.

(Reform of the consumption tax)

The consumption tax rate will be raised from 3 per cent to 5 per cent (including the rate of the local consumption tax) on 1, April 1997.

Preferential treatment for small businesses shall be amended so as to make the consumption tax system fairer and more credible.

※ For example, the special deduction system for small businesses will be abolished in 1997.

Appendix I-5

D Points of Corporate Taxes Reform, etc. (FY 1998, etc.)

1. Temporary Income Taxes Reduction in FY 1998

- (1) Total amount of Tax Reduction
 - ① Individual Income Tax (National Tax) – 1.4 trillion yen
 - ② Individual Inhabitants Tax (Local Tax) – 0.6 trillion yen
- (2) Method and Amount of Tax Reduction: fixed amount deduction

	National Tax	Local Tax	Total
Taxpayer	18,000yen	8,000yen	26,000yen
Spouse	9,000yen	4,000yen	13,000yen
Dependent	9,000yen	4,000yen	13,000yen
Typical Household*	45,000yen	20,000yen	65,000yen

* A married couple with two children

- (3) Additional Temporary Tax Reduction (See Appendix V)

2. Corporate Income Taxation

- (1) Reducing Tax Rates of Corporation Tax (National Tax)

	Before	Present
Standard Rate	37.5%	34.5%
Reduced Rate for Small and Medium-Sized Companies*	28%	25%
Reduced Rate for Cooperative Associations, etc.	27%	25%

(Note) This reduced rate is applied to the annual income (not more than 8 million yen) of corporations with capital that is not more than 100 million yen.

- (2) Reducing Tax Rates of Corporation Enterprise Tax (Local Tax)

	Before	Present
Standard Tax Rate for Ordinary Corporations	12%	11%
Standard Tax Rate for Special Corporations (Cooperative Associations, etc.)	8%	7.5%

- (3) Broadening the Tax Base
 - Abolition of reserve for bonus, reserve for guarantee of product
 - Reserve for bad debts, except for small-and medium-size enterprises, the statutory deductible rate is abolished. The special measure of the additional deductible rate for small-and medium-size enterprises is extended for three years.
 - Reserve for retirement allowance (Maximum accumulated amount: 40% →

- 20% of the total of retirement payable at the end of the accounting period)
 - Reserve for special repair. The accumulation rate is reduced, which is then incorporated into the special taxation measure.
 - Depreciation
 - Only the straight line method will be applied to newly-obtained buildings
 - Shortening of the useful life of buildings
 - Restriction of petty sum depreciable assets (200,000 yen→100,000 yen)
 - Abolition of simplified method of depreciation
 - Restriction of amortization of goodwill, etc.
 - Finance lease (The straight line depreciation method during lease period is applied to the nonresident's assets for non-domestic business)
 - Abolition of method of valuation of securities as accounting price or market price, whichever is lower
 - Introduction of percentage of completion method as revenue recognizing standard construction project whose contract value stands at ¥5 billion or more and takes two years or longer before completion.
 - Abolition of installment basis, except for installment sales with an installment period of two years or longer.
 - Entertainment expenses (Rate of exclusion from expenses concerning small-and medium-sized businesses with million or less capital 10%→20%)
 - Directors' remuneration (exclusion from expenses concerning excessive salary paid to an employee who is a relative of a director)
 - Investment in kind (special treatment including for land (taxation reschedule rate is limited to 80%)) is abolished and certain overseas subsidiaries are excluded).
 - Exclusion of dividends from revenue (Excluding investment trusts over 75% of which can be managed with foreign securities, etc.)
 - Streamlining the special taxation measures
 - Special measures for income tax credit on interest and dividends (abolition)
 - Others (Foreign penalties, deferred assets)
- Note: Required revisions will be made for the income tax and the consumption tax.

3. Land Taxation

- (1) Land Value Tax
 - Suspended for the time being
- (2) Income Tax and Individual Inhabitants Tax on Capital Gains from Transfer of Land Held by Individual for Long-Term(more than 5 years)

Principle			→	For 3 years; 1998~2000		
Capital Gains (million yen)	Income Tax	Individual Inhabitants Tax		Capital Gains (million yen)	Income Tax	Individual Inhabitants Tax
~40	20%	6%		~60	20%	6%
40~80	25%	7. 5%		60~	25%	7. 5%
80~	30%	9%				

(3) Additional Tax on Capital Gains from Transfer of Land Held by Corporations

Holding Period	Before	Present	Period of Suspension
5years~	5%	suspension	1998~2000
2years~5years	10%	suspension	1998~2000
~2years	15%	abolition	1998~

Appendix I-6

E Points of Permanent Tax Reduction, etc. (FY 1999, etc.)

1. Permanent Tax Reductions, etc.

(1) Personal Income Taxation

① Reduction in the Highest Marginal Tax Rate

—Personal Income Tax (National): taxable income of over ¥30 million—50%

→Taxable income of over ¥18 million—37%

—Inhabitant Tax (Local) : taxable income of over ¥ 7 million—15%

→Taxable income of over ¥ 7 million—13%

② Proportional Tax Reductions

a. Income tax

Tax credit is equivalent to 20% of the amount of the annual income tax, (Maximum ¥250,000).

b. Individual inhabitant tax

Tax credit is equivalent to 15% of the amount of the annual individual inhabitant tax, (Maximum ¥40,000).

③ Addition of exemption for dependents

a. Income tax

—¥50,000 is added to the amount of exemption for a specific dependent (a dependent from 16 to 23 years old. (¥580,000 before revision)

b. Individual inhabitant tax (applied since fiscal 2000)

—¥20,000 is added to the amount of exemption for a specific dependent (a dependent from 16 to 23 years old). (¥430,000 before revision)

(2) Corporate Income Taxation

① Reduction in Standard Tax Rates

	FY 1997	FY 1998	FY 1999
—Corporation Tax (National):	37.5%	→ 34.5%	→ 30.0%
—Corporate Enterprise Tax (Local) :	12.0%	→ 11.0%	→ 9.6%
→Combined Effective Tax Rate :	49.98%	→ 46.36%	→ 40.87%

② Reduction in Special Tax Rate for Small and Medium Enterprise

	FY 1997	FY 1998	FY 1999
—Corporation Tax:	28%	→ 25%	→ 22%
—Corporate Enterprise Tax:	6.0%	→ 5.6%	→ 5.0%

- These tax reductions will be applied for accounting periods beginning on and after 1 April 1999.

2. Housing-and Land-related Tax Measures

- (1) Introduction of Tax Credits for the Housing Loan The current tax credit for housing loans will be revised as follows, when applied for the next two years.
 - ① Extension of the deduction period 6 years → 15 years
 - ② Increase in the ceiling for loans outstanding 30 million yen → 50 million yen
 - ③ Tax credit rates: First to sixth years: 1%
Seventh to eleventh years: 0.75%
Twelfth to fifteenth years: 0.5%
→ Maximum amount of tax credit: 5,875 million yen in total
0.5 million yen per year for the first six years
(Current maximum amount: 1.7 million yen in total)
 - ④ Loans for acquisition of land, purchased together with a house, will also qualify for the above mentioned tax credit.
 - ⑤ The upper limit on floor space (240 m²) will be eliminated.
 - ⑥ Taxpayers who choose to carry over capital losses for their residential property will also be entitled to this tax credit. (Prior to this year, taxpayers have had to choose either the tax credit or the carry-over loss.)
- (2) Personal Income Taxes on Capital Gains from the Transfer of Land Personal Income taxes on capital gains from the transfer of land held for more than five years will be reduced (for the next two years).
Up to 60 million yen : 26% (including 6% Inhabitants Tax) →
Up to over 60 million yen : 32.5% (including 7.5% Inhabitants Tax)
On all gains 26% (including 6% Inhabitants Tax)

3. Tax Measures Related to Financial Markets

- (1) To promote international use of the Yen, the following measures will be taken:
 - Exempting withholding tax on interest from government bonds in the Bank of Japan book entry system paid to nonresident individuals and foreign corporations (Effective for interest in an interest calculation period beginning on or after 1 September 1999).
 - Exempting withholding tax on original issue discounts for TBs and FBs (Effective for TBs and FBs to be issued on or after 1 April 1999)
(Measures to ensure tax compliance will be introduced together with the above measures.)
- (2) The securities Transaction Tax and Bourse Tax will be abolished on 31 March 1999.

The special measure for listed stocks to allow taxation at 1.05% on proceeds of sales in lieu of taxation at 26% on capital will continue to be applied until 31 March 2001, and will then be abolished.

- (3) The special corporation tax (imposed on assets contributed by employers for corporate pension plans, etc. with a tax rate of 1%,) will be suspended for two years, considering the difficult situations for corporate pension plans that complement public pension systems.

Appendix I-7

FY 2002 Tax Reform (Main Points)

Ministry of Finance

19 December 2001

With a view to contributory to the structural reform, the FY 2002 Tax Reform will take measures outlined below including creation of a consolidated taxation system and necessary revision in taxation of SMEs and taxation related to financial/stock markets, taking account of the recent socio-economic changes and the severe fiscal situation.

Note: The permanent tax reductions (national and local) for individuals and corporations, which substantially exceed ¥6 trillion, will continue in FY 2002.

Consolidated taxation system

A consolidated taxation system will be created.

Basic thinking

- A consolidated taxation system is a system whereby the Corporation Tax will be charged on the integrated amount of profit and loss of a group of corporations.
- Introduction of a consolidated taxation system will facilitate restructuring of corporations and contribute to maintaining and strengthening global competitiveness of Japanese corporations as well as implementing structural reform of the economy.

Scope of corporations and the method of application

- The scope of corporations is a parent company and its 100% domestic subsidiaries.
- Application of the tax system is optional and subject to approval by the Commissioner of the National Tax Agency. Once elected, the tax system should continue to be applied.

Calculation of consolidated taxable income and consolidated tax liability

- The amount of consolidated taxable income and tax liability will be computed for the consolidated group of corporations as a single tax unit by applying necessary adjustments to the amount of taxable income of each corporation in

the consolidated group.

- Then, the amount of consolidated tax liability will be allocated to each corporation in the group based on the taxable income and loss of each corporation.

Application of taxation treatments

- Various tax treatments will be applied under the consolidated system, based on the principle of calculating the taxable income and tax liability for the group as a single tax unit, while making necessary adjustments taking account of the purpose of each taxation provisions.

Anti-tax avoidance rules

- A comprehensive anti-avoidance rule will be introduced in order to deal appropriately with various types of possible tax avoidances.

Application

- The system will be applied from business years beginning on or after 1 April 2002 and ending on or after 31 March 2003.

Measures to make up possible revenue loss

- Various measures to make up possible revenue loss (limited application of consolidated taxation in the consolidated system and broadening of corporation tax base) will be taken. The total review of these revenue measures will be made 2 years later.

SMEs

Relax of special additional tax on retained earnings of family (closely-held) corporations

- Add certain small and medium venture corporations to the scope of corporations eligible for non-imposition of the special additional tax.
- Discount the additional tax amount for SMEs by 5%.

Increase the cap for deductible entertainment expenses

- Fixed amount cap for deductible entertainment expenses of SMEs with capital of over ¥10 million but not exceeding ¥50 million will be increased to ¥4 million (currently ¥3 million).

Reduce the taxable value of non-quoted stocks in calculating inheritance tax

- The taxable value of non-quoted stocks inherited by individuals will be re-

duced by 10% in calculating inheritance tax.

Note: Applicable for assets inherited by inheritance or by bequeath on or after 1 January 2002.

Financial/stock markets

Reform tax exemption of interest income on certain small deposits

- Exemption of interest income on small deposits owned by the elderly, the disabled persons, etc. (Rojin Maruyu) will be reformed (in January 2006) and applied only to small deposits owned by disabled persons, etc..
- The elderly persons will be excluded from this treatment at the end of CY 2005 after applying transitional measures (for example, setting up new tax free account will not be allowed after January 2003).

Introduce special measures for simplified filing and optional non-filing of returns of capital gain of listed stocks held in a designated account.

- Capital gain of listed stocks held in a designated account will be calculated independently from those held in other account(s) —simplified filing of returns.
- Capital gain of listed stocks in the designated account may be taxed by election through withholding of tax at source and, in this case, no filing of a tax return will be required.

Broadening the scope for eligible stock options under the stock option taxation treatment in response to the changes of the Commercial Code

- The scope of recipients of eligible stock options will be broadened¹ and the limitation on the amount of exercised stock options will be increased (from currently ¥10 million to ¥12 million).

Exemption of tax on loan interest of cross-border repo

- Exempt from tax under certain conditions on loan interest of cross-border bond repurchase transactions (repo) between financial institutions.

Treatment on capital gain/loss of “treasury stocks”

- Capital gain or loss of “treasury stocks” (stock acquired by an issuing corporation) will be treated as increase or decrease of capital reserve (i.e. no taxable gain or loss will result)”

¹ It will include employees of 50% subsidiaries and sub-subsidiaries.

Coping with socioeconomic changes

Land and housing

- The tax rate of registration and licensing tax applicable to acquisition of a qualified fireproof high-medium rise building and its premises will be reduced to 2.5% (in principle 5%).
- Qualified repair and renovation of house to meet safety standards for earthquake will be added to the scope of eligible addition and betterment of residential houses for housing loan tax credit.

Environment/welfare

- Equipments for drying used timbers, those for food recycling into oil, and those for food recycling into methane gas will be added to the list of eligible equipments for special depreciation. The application of this special depreciation for recycling equipments will be extended by 2 years after making necessary adjustments.
- Extend the application of special depreciation for facilities caring the disabled people by 2 years.
- Reduce the taxable value of certain forests inherited by individuals by 5%. (NB. Applicable for assets inherited on or after 1 January 2002).
- Reimburse the amount of the Motor Vehicle Tonnage Tax corresponding to the remaining period of the automobile inspection certificate after the date of dismantling of used cars confirmed in accordance to the “manifest system” that will be introduced under the law for used automobile recycling. (NB. Applicable after enactment of the law for used automobile recycling).

Okinawa

- Accredited newly established corporations in a special financial operation zone that satisfy certain conditions—including operating their financial or financial related businesses in this special zone and employing constantly 20 or more employees in the zone—will be given a special income deduction of 35% for income arising from the business in this zone for 10 years from the date of establishment.
(The amount of special income deduction is limited to 20% of total amount of employment cost incurred in the zone. It is applicable alternatively to the special investment tax credit².)
- Extend the reduction in aviation fuel tax for flights to and from Okinawa by 5 years.

² Investment tax credit may alternatively be applied by election for acquisition of certain buildings and equipments of the accredited corporations in the zone.

Others

- Introduce a special tax-free reserve for exhibition at the 2005 World Exposition in Japan.
- In response to the changes made to the law for building a Shinkansen bullet train network across the country that will oblige creating a reserve for special large-scale renovation of Shinkansen, introduce a tax-free reserve for this renovation.
- Exclude certain sponsored research carried out by private universities, etc., from the scope of taxable profit-making activities of Corporations in Public Interest.
- Add the following corporations established under the Civil Code to the scope of corporations officially recognized as contributing to public welfare, donations made to which are tax deductible; (i) accredited corporations helping victims of crimes, etc., (ii) accredited corporations aiming at promoting sports for disabled people and helping other organizations that are conducting on a nation-wide basis, sports activities for disabled people.

Other Special Taxation Measures

While applying truly necessary measures, streamline special taxation measures with a view to making taxation appropriate.

(Reference)

FY 2002 Tax Reform (Initial Year)
(Tentative estimation of revenue changes made by the reform)

(¥100 million)

1. Consolidated taxation	-210
2. SMEs	-100
3. Others	140
<hr/> TOTAL	<hr/> -170

Note: Revenue change by introduction of consolidated taxation is —¥30 million inclusive of revenue increase resulting from the streamlining of special taxation measures under the heading “3. Others).

(“—” represents minus)

Appendix I-8

FY2003 Tax Reform (Main Points)¹

Ministry of Finance

In order to establish a desirable tax system to achieve sustainable invigoration of the economy and society, while taking into account the current economic and fiscal environment, the FY2003 tax reform will take the following measures outlined below:

- R&D tax credit and IT investment incentives to improve competitiveness of the Japanese Industry,
- Measures to 'integrate' inheritance and gift taxes from the viewpoint of facilitating the transfer of assets from the older generation (i.e. parents) to the younger generation (i.e. children), and tax rate cuts,
- Reduction and simplification of taxation of financial transactions and stocks for promoting the shift 'from deposits to investment',
- Tax rate cut of Registration and licence taxes (transaction tax) for promoting utilization of lands,
- Abolish 'special allowance' for spouse (exceeding the amount of 'allowance for spouse') from the viewpoint of integrating numerous personal deductions,
- Reducing the tax exempt threshold (¥30 mil) and the eligible vendors for the simplified regime (¥200 million) of consumption tax in order to improve trust and transparency of the system,.
- Review liquor and tobacco taxes, and
- Other relevant measures.

These measures will result in tax reduction amounting to about 1.5 trillion yen* in fiscal 2003, and achieve revenue-neutral tax reforms over several years.

Note: The permanent tax reductions (national and local) for individuals and corporations, which substantially exceed 6 trillion yen (introduced in fiscal 1999) will continue in FY2003.

* About 1.8 trillion yen including local taxes

R&D Tax Credit / Investment Tax Incentives

From the viewpoints of strengthening the global competitiveness of Japanese businesses, a new framework for R&D tax credit and focused investment incentives shall be introduced.

¹ The Japanese Fiscal Year begins in April and ends in March. The taxable year for corporations is the businesses year and for individuals it is a calendar year.

* www.mof.go.jp

R&D Tax Credit (proportional)

A new proportional R&D tax credit shall be introduced as an alternative¹ to the existing incremental R&D tax credit.

- For R&D activities conducted by corporations, a proportional R&D tax credit of 8% plus 2% (applicable only for FY 2003 to FY2005) of the amount of R&D expenditure shall be introduced.
 - For corporations with a higher proportion of R&D expenses, up to 2% of additional tax credit shall be applied.
- For R&D activities conducted by SMEs, a proportional tax credit of 12% plus 3% (applicable only for FY 2003 to FY 2005) shall be introduced.
- For R&D activities conducted jointly by academic, business and government circles, or R&D commissioned by the government, in order to promote basic studies or innovative studies, a proportional tax credit of 12% plus 3% (applicable only for FY 2003 to 2005) shall be introduced.
- The scope of qualified R&D expenses shall include such expenses as labor, non-personnel expenses and depreciation for machinery and buildings and expenses of R&D activities conducted overseas.
- The amount of the R&D tax credit shall not exceed 20% of the amount of corporation tax.
- The amount of the R&D tax credit exceeding the ceiling may be carried-over for one year under certain conditions.

Investment Incentives (IT)

Since IT investment would create immediate demand and promote improved industry competitiveness in the mid to long term, the investment incentives outlined below shall be applied for FY2003 to FY2005

- Scope of qualified IT investment to include both hardware and software
- Certain expenses for leasing may be eligible
- Corporations may elect tax credit (10%) or special allowance for accelerated depreciation (50%)
- The amount of tax credit shall not exceed 20% of the amount of corporation tax.
- Tax credit exceeding the ceiling may be carried-over for one year under certain conditions.

Accelerated depreciation for R&D investment

- In addition to the R&D tax credit (above), a special allowance (50%) shall be applied for R&D investment in FY2003 to FY2005.

Taxation of financial assets and stocks

- Special additional tax measures to promote a shift from deposits to investment (stocks) will be taken:
 - Dividends of stocks and distribution from publicly traded stock investment funds will be taxed at the reduced rate of 10% by withholding for five years² (see below).³
 - Capital gains of listed stocks will be taxed at the rate of 10% for five years⁴.
- From the viewpoint of creating simplified taxation of financial assets to ensure neutrality among them, taxation of stocks and publicly traded stock investment funds shall be streamlined and the usability of the "special account" for stocks shall be improved on a permanent basis.
 - Dividends of listed stocks will be taxed (by election) at the rate of 20% by withholding (after the running of five years mentioned above).
 - Loss arising from publicly traded stock investment funds can be aggregated with capital gain, if any, of stocks.
 - A new type of special account system will be introduced under which tax will be paid by withholding and no filing of returns will be required.
- Exemption from withholding tax on interest of qualified public bonds and corporate bonds (e.g. public bonds traded through the 'furiketsu' clearing system) received by corporations with capital of Y100million or over. (Applicable for interest of qualified bonds arising from the period of interest calculation starting on or after 1 April 2003).

² Dividend of stocks: Apr 2003-Mar 2008, Distribution from publicly traded Stock Investment Funds: Jan 2004-Mar 2008

³ No obligation to file returns applies for dividends and distributions taxed by 10% withholding.

⁴ Jan 2003-Dec 2007

Taxation of land

In order to promote utilization of lands, the tax rates of registration and license taxes (transaction tax) shall be reduced.

(Example)

Tax Rates	Transfer by sales
Current	5%
FY2003 to FY2005	1%
After FY2006	2%

Note: The existing special tax measure applicable to land transfer only shall be abolished.

SMEs

Given the current severe economic environment surrounding SMEs, the following measures shall be applied.

- Higher rate (12% plus 3%) of R&D tax credit (mentioned above)
- Application of an additional tax on retained earnings of family corporations (i.e. closely held corporations) shall be suspended for SMEs with low levels of equity capital for FY2003 to FY2005.
- The scope for immediate write-offs for small amount depreciation assets purchased by SMEs shall be broadened from Y100, 000 to Y300,000 for FY2003 to FY2005
- Investment in qualified 'ventures' may be deducted from the capital gain of stocks of the same taxable year.

Inheritance and gift taxes

Introduction of a new system for adjusting gift tax at the time of inheritance from the viewpoint of promoting the transfer of assets held by the older generation (i.e. parents) to the younger generation (i.e. children).

- A new system to calculate gift and inheritance taxes at the time of inheritance (applied by election) shall be introduced by deducting the amount of previously paid gift tax from the total tax amount calculated on the total amount of gifts and inheritance property.
 - Qualified gifts: The new system will be applied for gifts from parents of age 65 and older to children of age 20 and older
 - Exemption threshold at the time of receiving gifts: Gifts not exceeding Y25 million (in total) will be exempt from the tax objected property.
 - Tax rate at the time of receiving gifts: Prepayment of gift tax will be charged at the

rate of 20% on the amount exceeding the exemption threshold. The amount of gift tax will be treated as prepayment of tax against inheritance tax at the time of inheritance (refundable).

Additional exemption for residential housing

- A tax exemption threshold of Y35 million will be applied for gifts from parents (no age qualification applies) to children (20 years and over) for the purpose of purchasing residential housing until CY2005.

Tax rate cuts

- The top rates of inheritance tax (currently 70%) and gift tax (70% also) will be both reduced (to 50%)⁵.
- The number of inheritance tax brackets (currently nine brackets) and gift tax brackets (thirteen brackets) will be both reduced (to six)⁴.

Energy

- Petroleum tax on LPG and LNG will be increased, and shall be imposed on coal. Promotion of power-resources development tax (PPRDT) shall be reduced.

Petroleum tax	Current	Oct. 2003-Mar. 2005	Apr. 2005 to Mar. 2007	Apr. 2007-
on LPG	670/ton	800/ton	940/ton	1,080/ton
on LNG	720/ton	840/ton	960/ton	1,080/ton
on Coal	n/a.	230/ton	460/ton	700/ton

PPRDT	0.445/kwh	0.425/kwh	0.4/kwh	0.375/kwh
-------	-----------	-----------	---------	-----------

Individual Income Tax

From the viewpoint of broadening the tax base, abolish special allowance for spouse

- Among allowances applicable for spouses, the additional amount (maximum of Y380,000) shall be abolished from CY2004.

Consumption Tax

From the viewpoint of improving the transparency of the consumption tax, special treatments for small

vendors will be revised.

- Diminish the exemption for small vendors to the level one-third of the current level: Reduce the tax exemption threshold for eligible small vendors from Y30 million (current level) to Y10 million.
- Scale down the simplified tax scheme (i.e. the use of the deemed ratio for a purchase): Restrict eligibility for the application of the simplified tax scheme by lowering the ceiling from traders with annual sales of Y200 million or less to those with annual sales of Y50 million or less.
- Obligation to show net price: Vendors shall be obliged to show the net price (cost plus tax) of goods and services

Liquor

- Difference in tax rates on similar types of liquors shall be reduced through adjusting tax rates on low-malt beer (*happoshu*) wine, and others.

	Proposed change	Reference (tax rate for similar type of liquor)
Low-malt beer (<i>Happoshu</i> , Malt proportion ~ 25%)	(per KL) Increased to 134,250 yen from 105,000 yen (current level)	(Beer) 222,000yen
Wine	(per KL) Increased to 70,472 yen from 56,500 yen (current level)	(Sake, Alcohol 12%) 112,390 yen
Sake compound (Alcohol 15%)	(per KL) Increased to 94,600 yen from 79,300 yen (current level)	(Sake, Alcohol 15%) 140,500 yen
Sweet wine (Alcohol 12%)	(per KL) Increased to 103,722 yen from 98,600 yen (current level)	(Liquor) 119,088 yen

⁵ The tax bracket structure including 50% of the top tax rate for gift tax will be applicable where the above mentioned new system for calculating gift and inheritance taxes is not elected.

Taxation of Corporations by the Size of Their Businesses (local tax)

From the viewpoints of sharing the tax burden more broadly and thinly and clarifying the relationship between the burden and benefits in the local community, taxation of corporation by the size of their businesses shall be introduced:

- Taxpayers: corporations with capital of Y100million and over.
- Tax base: Changing the tax base from the profits of corporations to a mix of profits and capital and other value added items such as wages, interest and rentals. Special measures to reduce tax burden for corporations with high proportion of wages in their value added and those with significant amount of capital shall be taken.
- Tax rates: income (7.2%), value added (0.48%), capital (0.2%)
- Applicable for taxable year beginning after FY2004.

(Reference)

FY2003 Tax Reform (Initial Year)
Tentative estimation of revenue changes made by
the reform
(Inland Revenue, National)

(Y100 Million)

1 Taxation of Corporations	- 13,040
(1) R&D (excluding (3) below)	-5,470
(2) Investment incentives (excluding (3) below)	-5,270
(3) SMEs	-2,300
2 Inheritance and gift taxes	-1,030
3 Taxation of financial transactions and stocks	-960
4 Taxation of land	-2,100
Total of 1-4	-17,130
5 Income tax (individual)	n.a.
6 Consumption tax	n.a.
7 Liquor and tobacco taxes	+1,630
8 Others	+60
Total of 5-8	+1,690
Net of 1-8 above	-15,440
9 Petroleum tax	+140
10 Motor vehicle tonnage tax	-930
Total: General Account Revenue	-16,230
11 Promotion of power-resources development tax	-83
12 Motor vehicle tonnage tax*	+930
Grand Total	-15,383

*Earmarked for construction and improvement of local roads

Appendix I-9

FY2004 Tax Reform (Main Points)

Ministry of Finance
19 December 2003

With a view to contributing to sustainable invigoration of the economy and society, while taking into account the current economic and fiscal environment, the FY2004 tax reform will take measures in taxation of land and housing, SMEs, financial assets and stocks, corporation, and international transactions. Likewise, taking into account the view of contributing to reforms of social security systems, review of taxation of pensions for ensuring inter-generational fairness as well as fairness within the same generation. In addition, taking necessary measures to promote autonomy of local governments.

Notes:

1. The permanent tax reductions (national and local) for individuals and corporations, which substantially exceed 6 trillion yen, (introduced in FY1999) will continue in FY2004.
2. 1.5 trillion yen tax cuts (national and local) enacted in FY2003 will be applied in FY2004

Taxation of land and housing

Residential Houses

- Extend the application of tax credit for residential mortgages as follows

Year of inhabitation	Qualified amount of outstanding mortgage (QOM)	Amount of tax credit (% of QOM)
CY2004	Y50 million or less	1% (for year1 – year10)
CY2005	Y40 million or less	1% (for year1 – year8) 0.5% (for year9 – year10)
CY2006	Y30 million or less	1% (for year1 – year7) 0.5% (for year8 – year10)
CY2007	Y25 million or less	1% (for year1 – year6) 0.5% (for year7 – year10)
CY2008	Y20 million or less	1% (for year1 – year6) 0.5% (for year7 – year10)

- Extend the application of losses carried forward from the replacement of residential houses. The sold house does not have to be mortgaged. The application of the special tax rate will be extended for 3 years.
- Introduce new losses carried forward from the sale of mortgaged residential houses.

Land

- Long term capital gains of land and housing
 - The tax rate of income tax for long-term capital gains on the sale of land and housing will be reduced from 26% (current level) to 20% (national 15% and local 5%).
 - The special tax rate of income tax for capital gains on land for creation of high-quality residential land will be reduced to 14% (up to 20 million yen). The application of the special tax rate will be extended for 5 years.
 - Abolish special deductions (Y1 million) for long term capital gains
- The tax rate of income tax for short-term capital gains from the sale of land and housing will be reduced to 39% (national 30% and local 9%).
- Aggregation of capital gains and losses from the sale of land and housing with other items of income will be abolished.

Note: These measures will be applied for sales made on or after 1st January, 2004.

Taxation of SMEs

- The income tax rate on capital gains of unlisted stocks will be reduced from 26% (current level) to 20%.
- The scope of qualified "ventures" for the purpose of reduced taxation of income tax under the "angel taxation"¹ system will be expanded to include investment in ventures through certain 'green sheet listed' investment funds and security corporations.
- The amount of certain stocks of family owned SMEs that are eligible for a special reduced calculation of inherited assets for the purpose of inheritance tax will be increased to Y1,000 million (currently Y300 million)
- Gain on the sale of inherited unlisted stocks to the issuing corporation for the purpose of paying inheritance tax will be taxed as capital gains, rather than deemed to be dividends.²

Taxation of Financial Assets and Stocks

- Capital gains on open stock investment funds (stock-type investment trusts) will be taxed at the same reduced rate as capital gains of stocks.
 - Apply reduced rate of 10% (national 7%, local 3%) on capital gains (applicable from Jan 2004)
 - Capital losses may be carried forward for 3 years.
 - Added to the scope of assets that may be held in a "special account" under which tax will be paid by withholding and the filing of returns will not be required.
- The tax rate on capital gains of unlisted stocks will be reduced to 20%. (Repeat of item mentioned above)
- Banks will be allowed to operate "special accounts".

Corporations

- Extend the period for losses carried-forward from 5 years (currently) to 7 years.
 - This will be applied retroactively for three previous taxable years (ie. businesses years beginning on or after 1st April

2001).

- Periods of statutory limitations and book keeping obligations will be extended.
- Abolish the 2% additional tax for corporations electing consolidated taxation

International Taxation

- Implement new Japan-US tax treaty by introducing new domestic legislation reflected by an updated tax treaty policy.
 - Clarify taxation and its procedures on business entities that are subject to different tax treatments in Japan and in the other contracting state.
 - Introduce procedural rules for applying treaty benefits only to residents in contracting states who satisfy the criteria for the benefits.
- Further exploration of bilateral tax treaties with other countries.

Pensions

- With the view of contributing to pension reform, review taxation of pensions to promote fairness among generations and within cohorts:
 - The additional part of public pension deduction for persons age 65 and over will be abolished.
 - Likewise, exemption for the elderly (Y500,000) will be abolished.
 - A special additional guaranteed amount of public pension deduction (Y500,000) will be introduced as consideration for pensioners with only standard amounts of pension income.
(These measures will be applied from CY2005)

References:

- Minimum amount of income subject to income taxation for a household with a couple (aged 65 and over): Y2,053 thousand/p.a.
- Standard amount of pension benefits
 - Employee pensions: Y2,035 thousands /p.a.
 - Basic pension: Y797 thousands /p.a.

(p.t.o)

¹ Angel taxation: Only half of the capital gains of the sale of stocks of qualified ventures are taxed. The amount of investment in qualified ventures is deductible from the amount of capital gains of stocks in the same taxable year.

² Under income tax, a deemed dividend is taxed at progressive rates while capital gains is taxed at a flat rate

- Increase the limitation on the amount of contribution to the Defined Contribution Pension (DCP) for employees to encourage self-help efforts by employees.

	Contribution by employees only	Contribution by employers only	
		Employees not covered by other occupational pensions	Covered by occupational pensions
Current level	Y180,000 /p.a.	Y432,000 /p.a.	Y216,000 /p.a.
Reform	Y216,000 /pa	Y552,000 /p.a.	Y276,000 /p.a.

Local governments and local taxes

- As part of "three part reform", carry out full-fledged transfers of part of 'tax revenue sources' from individual income tax (national tax) to local inhabitants tax by FY2006. As a bridging measure, introduce local transfers of income tax (Y424.9 billion) in FY2004, which will be shared by local governments in proportion to population size.

Note: Per capita rate local inhabitants tax will be applied to a wife whose husband is paying per capita rate inheritance tax (such a wife is exempt from payment of the tax).

(Reference)

FY2004 Tax Reform (Initial Year)
Tentative estimation of revenue changes made by the reform
(Inland Revenue, National)

	(Billion Yen)
Taxation of land and housing	-4
SMEs	-1
Corporation tax	-53
Pension	+39
Streamlining of special taxation measures (corporation tax)	+10
Subtotal	-9
Local Transfer of income tax	-425
Net of items above	-434

Appendix I-10

FY2005 Tax Reform (Main Points)

Ministry of Finance
20 December 2004

With a view to establishing a 'desirable tax system' that will contribute to sustainable invigoration of the economy and society, while taking into account the current economic and fiscal environment and having a vision for anticipated review of individual income taxation at national and local levels in the FY2006 tax reform, the FY2005 tax reform will reduce the benefits of the proportional across-the-board tax credit and take measures in taxation of housing, financial assets and stocks, international transactions and SMEs.

Individual income taxation (national and local)

- FY2005 reform: Based on directions given in the Outline of FY2004 Tax Reform of the ruling coalition (Dec 2003), half of the benefits of the across-the-board tax credit will be reduced
(Income Tax) Applicable from 2006
 - The rate of tax credit will be reduced from 20% to 10%
 - The ceiling on the tax credit will be reduced from ¥250,000 to ¥125,000(Local Inhabitants Tax) Applicable from 2006
 - The rate of tax credit will be reduced from 15% to 7.5%
 - The ceiling on the tax credit will be reduced from ¥40,000 to ¥20,000

Housing

- The scope of old houses qualifying for special tax treatments (such as tax credit for residential mortgages) will be expanded to include certain old houses that satisfy anti-earthquake safety standards, irrespective of the limitation on the number of years from construction (ie. 20 years for non-fire proof housing and 25 years for fire-proof housing).

Taxation of financial assets and stocks

- Stocks held outside of security corporations may be deposited in a new type of special account system by election (applicable for stocks the actual purchase price of which is available).
- A new measure will be introduced to treat the book value of stocks deposited in the new type of special account system as capital loss where the economic value of such stocks becomes nil.

International Taxation

- Deductible period for dividends from foreign subsidiaries whose retained earnings were taxed under the anti-deferral rules for controlled foreign corporations (CFC rules) will be extended from 5 years to 10 years. Overseas companies, which mainly operate in a resident country and are effectively managed there, will be allowed to deduct 10% of their direct personnel expenses from the taxable retained earnings under the CFC rules.
- Procedural requirement for interest tax exemption for non-resident holders of the Japanese Government Bond (JGB) will be streamlined.
- Capital gains derived from the sale of stocks or other comparable rights in a company which derives at least 50% of its value directly or indirectly from real property in Japan will be taxed in Japan.
- Capital gains derived by a partnership from the sale of stocks or other comparable rights in a company will be taxed in Japan, if that partnership holds 25% or more of the entire share capital of the company and if it alienates 5% or more of the entire share capital during the year.
- Allocable income to a non-resident partner, which is earned through partnership activities in Japan, will be withheld at 20% tax rate on a net profit every year.

Decentralization

- As part of the 'three-part-reform' (reforms of subsidies, local allocation tax and transfer of tax revenue sources from national to local governments), the carry out full-fledged transfer of tax revenue sources from Income Tax (national) to Local Inhabitation Tax.
- As a temporary measure, transfer ¥1,115.9 billion as local transfer of income tax to local governments. (3/5 shall belong to prefectural governments and 2/5 shall belong to townships and villages. Each local government shall receive the transfer in accordance with its population).

SMEs and Entrepreneurships

- Application of special tax treatment (tax on capital gain will be reduced by half) for qualified sale of stocks of qualified 'ventures' will be extended until FY2006 ('Angel' taxation).

Others

(Promoting activities of non-profit making organizations)

- The scope for qualified NPOs will be relaxed
 - Apply 'public support' through the averaging of donations/subsidies received in the past two years (currently the condition must be met in each taxable year).
 - Simplify documentation for applying the status as qualified NPOs and information reporting obligations.
- Increase the limitation of deductions for donation under income tax (25% of taxable income to 30% of the same).

(Restructuring of corporations)

- When liquidation of a corporation under the Civil Rehabilitation Law or certain private arrangements are conducted, the following special treatments will be given to the debtor corporation: (i) appraisal gain/loss of the corporation shall be taxed/deducted and (ii) carry-over of loss of the corporation arising from taxable years prior to the past 7 taxable years (i.e. limitation for carry forward of loss) may be deducted against the taxable gains of the corporation from forgiveness of debts by its creditors.

(Human Investment tax credit)

- A new tax credit (25% of the increased amount of expenditure of corporations for training employees) will be introduced. For small corporations, larger benefits will be given.

(Deduction for social insurance premiums)

- For the purpose of applying deductions for social insurance premiums, it will be made obligatory to attach a copy of national pension premium receipts when filing tax returns.

* * *

(Reference)*

FY2005 Tax Reform
Tentative estimation of revenue changes
implemented by the reform in FY 2005
(National)

(Billion Yen)

Reduction of the 'across-the-board' tax credit	+ 185
Housing	- 3
Other discretionary measures	
- Corporations	- 10
- Individuals and others	- 1
Subtotal	+171
Local Transfer of income tax	- 691
Total	- 520

*Rounded figures and provisional estimation.

Appendix I-11

FY2006 Tax Reform (Main Points)

Ministry of Finance
20 December 2005

With a view to establishing a 'desirable tax system' that will contribute to sustainable invigoration of the economy and society, while taking into account the current economic and fiscal environment, the FY2006 tax reform will abolish the proportional across-the-board tax credit, transfer substantial tax revenue sources from national Income Tax to Local Inhabitant Tax, and take measures in areas including corporate taxation, taxation of land and housing, international taxation, liquor tax and tobacco tax.

Individual income taxation

- As a part of the 'three-part-reform' (integrated reform of subsidies, local allocation tax and transfer of tax revenue sources from national to local governments), transfer substantial tax revenue sources of ¥3 trillion from national Income Tax to Local Inhabitant Tax. Consequently, the progressive rate structure of Income Tax will be reformed into 6 brackets structure with tax rates ranging from 5% to 40%*.

* This new rate structure will be applied to Income Tax from CY2007. In FY 2006, transfer of tax revenue sources will be carried out through Income Transfer Tax as a temporary measure.

- The remaining half of the across-the-board tax credit (10% of Income Tax up to ¥125,000 and 7.5% of Local Inhabitant Tax up to ¥20,000) will be abolished from CY2007 (for Local Inhabitant Tax, from FY2007).

Corporate taxation

- The current special tax credit for R&D expenses selective on total or incremental amount will be streamlined into a credit based on total with a new additional credit for 5% of the amount exceeding 'comparable R&D expense' as a temporary measure applicable for 2 years.
- To help strengthen information infrastructure for businesses, establish a tax incentive to allow corporations, in acquiring equipments that would improve competitiveness and further strengthen information infrastructure, either special depreciation of 50% of the standard acquisition value or special tax credit of 10 % of that value, as a temporary measure applicable for 2 years.
- Taxation on retained earnings of family corporations will be reviewed fundamentally by substantially reducing the scope of family corporations and expanding the deductible amount under the tax.

- In treating entertainment and social expenses as non-deductible expense, cost of drinking and eating not exceeding ¥5,000 per person will be excluded from the non-deductible amount.
- As regards the tax incentive for SMEs to facilitate investment, certain software and digital Multi Function Peripherals (MFP) will be added to the qualified assets, and its application will be extended for 2 years.

Taxation of land and housing

- Registration and License Tax on transactions such as purchase and sales of lands will be reduced.
- Introduce a new special income tax credit for repairs to houses to improve earthquake resistance (for 10% of the cost, up to ¥200,000).
- Application of the special treatment in calculating at the time of inheritance gift tax and inheritance tax on funds for purchasing houses will be extended for 2 years.

International taxation

- Take measures to promote international investment and prevent international tax avoidance, including review of the 'non-permanent resident' scheme and thin-capitalization rule, as well as expand the investigation authority to acquire information under the information exchange provisions of tax treaties.

Liquor tax and tobacco tax

- Streamline the classification of alcoholic beverages (liquor) for the Liquor Tax into major 4 categories: 'sparkling', 'fermented', 'distilled' and 'hybrid' liquors. The tax rates will be simplified accordingly *.
- *This reform will be implemented from 1 May 2006.

- Raise tobacco tax rate to ¥0.426/piece (¥0.852/piece totaled with local taxes)*.
*This rate will be applied from 1 July 2006.

* * *

Measures responding to the social and economic changes

- Modify the income deduction for casualty insurance premiums to introduce deduction for earthquake insurance premiums (up to ¥50,000).
- Decrease the non-deductible amount of the income deduction for contributions and donations from ¥10,000 to ¥5,000.
- Abolish public notice system for tax returns under income tax and other taxes.
- Allow electronic issuance of withholding slips and certain other tax documents.
- Take necessary measures in accordance with the enactment of the new Corporate Law.

Others

- In-kind payment of inheritance tax will be reviewed. The changes will include clarification of non-eligible properties, clarification of the required procedure, and legal provisions governing the period of examination of application.

(Reference)*

Preliminary estimates of revenue impacts of FY2006 Tax Reform
(in initial year; national internal taxes)

(Billion Yen)	
Individual income tax (reduction due to the transfer of tax revenue sources)	-443
Abolition of the across-the-board tax credit	+199
Corporate taxation	-257
Taxation of land and housing	-152
Tobacco tax	+71
Measures responding to the social and economic changes	-1
Other reforms of special taxation measures	+962
Others	+2
(Subtotal)	+381
Local Transfer of income tax	-1,893
Total	-1,512

*1. Total local transfer of income tax in FY2006 will amount to ¥3,009 billion: ¥1,116 billion by FY2005 tax reform plus ¥ 1,893 billion by FY2006 tax reform.

2. Figures are rounded and subject to changes.

Appendix II Summary of

Tax	Taxpayer	Tax Base
Income Tax: Income Tax Law	(1) Individual. (a) Resident taxpayer: Individual dwelling or residing for one year or longer in Japan, excluding non-permanent residents (see(b)).	<p>Total income—gross income less necessary expenses or employment income deductions—from sources in Japan and abroad.</p> <p>The employment income deduction is ¥650,000 when income receivable is not more than ¥1,625,000, 40% of income when exceeding ¥1,625,000 but not ¥1,800,000, 30% of income plus ¥180,000 when exceeding ¥1,800,000 but not ¥3,600,000, 20% of income plus ¥540,000 exceeding ¥3,600,000 but not ¥6,600,000, 10% of income plus ¥1,200,000 when exceeding ¥6,600,000 but not ¥10 million, and 5% of income plus ¥1,700,000 when exceeding ¥10 million.</p> <p>Retirement income: 50% of revenue deducted after subtracting a special deduction.</p> <p>Timber income: a standard deduction and a special deduction of ¥500,000 are allowed for taxable income (the amount of the timber income is divided by five and the tax amount due is obtained by multiplying the tax amount on that one-fifth by five).</p> <p>Capital gains: 50% of revenue deducted (in the case of short-term capital gains, rate is not 50%) after subtracting a special deduction of ¥500,000. Capital gains from the sale or transfer of land, buildings, or securities, however, are taxed separately from other income under the Special Taxation Measures Law as mentioned below.</p> <p>Occasional income: 50% of revenue deducted after subtracting a special deduction of ¥500,000.</p> <p>The following items are deductible from total income:</p> <p>(a) Deduction for casualty losses The larger one of (Losses from casualties – 10% of total income) or (Expenses related to casualties – ¥50,000).</p> <p>(b) Deduction for medical expenses Total Medical expenses – the smaller one of 5% of total income or ¥100,000. (Maximum ¥2,000,000)</p> <p>(c) Deduction for social insurance premiums</p> <p>(d) Deduction for premiums for small-scale enterprise mutual aid</p> <p>(e) Deduction for life insurance premiums Sum of the general life insurance premiums (The full amount of life insurance premiums if life insurance premium paid isn't over ¥25,000, a half of it + ¥12,500</p>

the National Tax System

Rate	Report & Payment
<p>(1) Total taxable income</p> <p>Not over ¥ 3,300,000 10%</p> <p>¥ 9,000,000 20%</p> <p>¥18,000,000 30%</p> <p>Over ¥18,000,000 37%</p> <p>※ (After 2007)</p> <p>Not over ¥ 1,950,000 5%</p> <p>¥ 3,300,000 10%</p> <p>¥ 6,950,000 20%</p> <p>¥ 9,000,000 23%</p> <p>¥18,000,000 33%</p> <p>Over ¥18,000,000 40%</p> <p>(2) Retirement income and timber income are taxed separately from other income. Interest income is taxed at the rate of 15% at the source (5% local inhabitants tax is levied in addition).</p> <p>(3) Tax credit for dividend income: 10% of dividend income (5% of dividend income for the part of the amount over ¥10 million) is credited with respect to the tax amount.</p> <p>(4) Tax credit for foreign income taxes: any foreign income tax or any counterpart of Japanese income tax accrued is creditable.</p> <p>(5) Proportional tax credit: 10% of the tax amount before the proportional tax credit (upper limit ¥125,000) Proportional tax credit was abolished in FY2006 Tax reform (applicable from 2007)</p>	<p>(1) Self-assessment system. Prepayment system is applied. Payments due: 1st installment 1-31 July 2nd installment 1-30 Nov. Final return due 16 Feb-15 Mar.</p> <p>(2) The withholding tax system is applied to the following income:</p> <p>(a) Employment income and retirement income according to the withholding tax tables</p> <p>(b) Interest and income from securities investment trust..... 15%</p> <p>(c) Dividend income..... 20% (7% for listed stocks)</p> <p>(d) Manuscript fee, remuneration for public entertainment, etc..... 10% for not more than ¥1 million and 20% for more than ¥1 million</p> <p>(e) Profits of anonymous association .. 20%</p> <p>(f) Profits from Redemption of Discount Bonds..... 18%</p> <p>Tax withheld must be paid to the Government by the 10th of the following month.</p> <p>* Note: For income prescribed in (b), (f) above, separate income taxation will be the final tax liability and is not subject to “aggregate income taxation.”</p>

Appendix II Summary of

Tax	Taxpayer	Tax Base
Income tax (Contd.)		<p>if it is over ¥25,000 and not more than ¥50,000, a quarter of it + ¥25,000 if it is over ¥50,000 and not more than ¥100,000, ¥50,000 if it is over ¥100,000) and personal pension plan premiums.</p> <p>(f) Deduction for casualty insurance premiums</p> <p>Long-term (10 years and longer) insurance; The full amount of casualty insurance premiums if casualty insurance premiums paid isn't over ¥10,000, a half of it + ¥12,500 if it is over ¥10,000 and not more than ¥20,000, ¥15,000 if it is over ¥20,000.</p> <p>Short-term insurance; The full amount of casualty insurance premiums if casualty insurance premiums paid isn't over ¥2,000, a half of it + ¥1,000 if it is over ¥2,000 and not more than ¥4,000, ¥3,000 if it is over ¥4,000)</p> <p>※ It is revamped to the “deduction for earthquake insurance premium” in 2007. The amount of insurance premium corresponding to earthquake-induced damages in a casualty insurance contract (maximum 50,000 yen) is deducted from the income.</p> <p>(g) Deduction for contributions or donations (the smaller of the amount of specified contributions or 30% of total income) –¥5,000.</p> <p>(h) Exemption for the handicapped ¥270,000 (for the severely handicapped ¥400,000)</p> <p>(i) Exemption for widow(er) or working students ¥270,000 (¥350,000 for specific widows)</p> <p>(j) Exemption for spouses ¥380,000 (¥480,000 for spouses who are 70 years old or older and eligible for exemption of elderly dependent relatives)</p> <p>(k) Special exemption for spouses ¥380,000 (Maximum amount)</p> <p>(l) Exemption for dependent relatives ¥380,000 for each dependent relative (¥480,000 for each elderly dependent relative 70 years old or older, ¥630,000 for a specific dependent relative from 16 to 22 years old)</p> <p>(m) Basic exemption: ¥380,000</p> <p>Total income derived from sources within Japan and other income paid in or remitted</p>

the National Tax System

Rate	Report & Payment

Appendix II Summary of

Tax	Taxpayer	Tax Base
Income tax (Contd.)	<p>(b) Non-permanent resident taxpayer: Resident who does not have Japanese nationality and has maintained a domicile or residence in Japan for no longer than 5 years of the past 10 years.</p> <p>(c) Non-resident taxpayer: Taxpayer other than a resident taxpayer.</p> <p>(2) Corporation, including non-juridical association, etc.</p> <p>(a) Domestic corporation: Corporation having its head or main office in Japan.</p> <p>(b) Foreign corporation: Corporation not having its head or main office in Japan.</p>	<p>to Japan</p> <p>In the case of aggregate income taxation: income-gross income less necessary expenses –from sources within Japan, no deduction or credit being given, except for the basic exemption, deductions for casualty losses, and for contributions or donations. In the case of the separate income taxation: gross income from sources within Japan. Interest, dividends, and remuneration for public entertainment received within Japan</p> <p>Gross income from sources within Japan.</p>
	Separate taxation of capital gains	
	Individual	<p>(1) Long-term capital gains (capital gains from land or buildings continuously owned by a taxpayer for over 5 years as of 1 January of the year in which the transfer was made)</p> <p>(2) Short-term capital gains (capital gains from land or buildings continuously owned by a taxpayer for not over 5 years as of 1 January of the year in which the transfer was made)</p> <p>(3) Capital gains derived from the transfer of securities etc.</p> <p>(4) Miscellaneous incomes, etc. related to dealing in futures.</p>

the National Tax System

Rate	Report & Payment
<p>Foreign corporations conducting business in Japan may receive the same treatment as domestic corporations. The rate is reduced or is nil under certain domestic tax laws and tax treaties.</p>	
from the transfer of land, buildings or securities	
<p>(1) Long-term capital gains Deductions: Increased deduction of ¥8 million to ¥50 million according to types of transfer or assets Method of taxation: 15% of T.L.C.G. [Note] T.L.C.G.: Taxable long-term capital gains</p> <p>(2) Short-term capital gains Deduction: Special deduction of ¥8 million to ¥50 million according to the type of transfer or assets Tax amount: 30% of the taxable short-term capital gains</p> <p>(3) Capital gains from the sale of securities: Method of taxation: 15% of the taxable capital gains 7% of capital gains derived from the sale of listed stocks, etc, from 2003 to 2007.</p> <p>(4) Miscellaneous incomes, etc. related to dealing in futures Taxation system: 15% of miscellaneous taxable incomes</p>	

Appendix II Summary of

Tax	Taxpayer	Tax Base
<p>Corporation Tax:</p> <p>Corporation Tax Law</p>	<p>(1) Domestic corporation</p> <p>(2) Foreign corporation having assets or business within Japan</p>	<p>Net income for each accounting period or liquidation income Net income for each accounting period from sources within Japan (With regard to the corporations in public interest, their income from profit-making business will be taxed.)</p> <p>(1) Non-taxable revenue items are:</p> <ul style="list-style-type: none"> (a) Profits from transactions of capital, etc. (b) Dividends received from domestic subsidiaries, 50% of the dividends in case of those from other domestic corporations. (c) Gains from revaluation of assets (d) Refunds of corporation tax, etc. <p>(2) Non-deductible expenses items are:</p> <ul style="list-style-type: none"> (a) Losses from the capital transactions (b) Losses from the revaluation of assets (c) Capital expenditures on immovable properties (d) The unreasonably large portion of directors' salary, etc. (e) Contributions exceeding one-half of the total of 2.5% of profits and 0.25% of capital (on an annual basis) (f) Corporation tax, prefectural tax and municipal tax (g) Expenses, penalties and fines on illegal activities (h) Entertainment expenses
<p>Inheritance Tax and Gift Tax;</p> <p>Inheritance Tax Law</p>	<p>(1) Inheritance Tax;</p> <p>The person having acquired properties through inheritance or bequest</p>	<p>(1) The total balance obtained by deducting Basic deduction (¥50 million) + number of legal heirs × ¥10 million) from the total property</p> <p>(2) On the assumption that legal heirs inherit properties in accordance with the statutory shares in succession by civil law, the total amount of inheritance taxes payable by the individual legal heirs and donees of bequests shall be obtained by multiplying the total amount of inheritance by the tax rate.</p> <p>(3) The tax amount payable by the individual heirs and donees of bequests shall be obtained by proportionately dividing the total inheritance as mentioned in (2) above in accordance with the amounts actually inherited by the individual heirs and donees.</p>

the National Tax System

Rate	Report & Payment
<p>(1) Tax rates for ordinary income</p> <p>Ordinary corporation</p> <p>(a) Corporations with capital more than ¥100 million 30.0%</p> <p>(b) Corporations with capital of no more than ¥100 million</p> <p>For annual income of more than ¥8 million 30.0%</p> <p>For annual income of no more than ¥8 million 22%</p> <p>For corporations in the public interest, cooperative associations, etc. 22%</p> <p>(2) Tax rates for liquidation income</p> <p>For ordinary corporations 27.1%</p> <p>For corporations in the public interest, cooperative associations, etc. 20.5%</p> <p>Notes: Capital gains from the transfer of land are subject to additional tax according to the holding period. However, it has been suspended until December 31, 2008.</p> <p>Not more than 5 years 10%</p> <p>Over 5 years 5%</p>	<p>Self-assessment:</p> <p>Taxpayers must file a return and pay the tax within 2 months of the end of an accounting period. A corporation whose accounting period exceeds 6 months is required to file an interim return.</p> <p>The income tax withheld on interest income or dividend income is deducted from the corporation tax due.</p>
<p>(Tax Rate)</p> <p>¥10 million or less 10%</p> <p>¥30 million or less 15%</p> <p>¥50 million or less 20%</p> <p>¥100 million or less 30%</p> <p>¥300 million or less 40%</p> <p>More than ¥300 million 50%</p> <p>(Tax Deduction)</p> <p>(1) Deduction for spouse</p> <p>A x B/C</p> <p>A: Total amount of inheritance tax</p> <p>B: The smaller of the following (a) or (b):</p> <p>(a) The statutory share of the spouse in succession out of the total properties inherited or donated (¥160 million in case the amount is less than ¥160 million)</p> <p>(b) The total property actually acquired by the spouse</p> <p>C: The total property acquired</p>	<p>(1) Tax payment by self-assessment</p> <p>(2) Time limit for tax payment:</p> <p>The taxpayer having acquired property through inheritance shall submit the declaration and pay the tax within ten months after inheritance.</p>

Appendix II Summary of

Tax	Taxpayer	Tax Base
<p>Taxation system for settlement at the time of inheritance</p>	<p>A child who is 20 years old or older who acquired a property through donation from a specified donor (his/her parent who is 65 years old or older) and selected the taxation for settlement at the time of inheritance.</p>	<p>(1) At the time of donation Tax shall be imposed on the part in excess of the special deduction (¥25 million: usable in two or more times unless the total amount exceeds the upper limit) on the property donated from a specified donor which is distinguishable from other donated properties.</p> <p>(2) At the time of inheritance The amount of inheritance tax shall be calculated by adding the donated property applicable to the taxation for settlement at the time of inheritance (see (1) Inheritance Tax for the method of calculation). Note: The price of the donated property to be added to the inherited property shall be in the current price as of the time of donation.</p>
	<p>(2) Gift tax (taxation for each calendar year) The person who acquired a property through donation</p>	<p>The basic exemption of ¥1.1 million is allowed from the total property acquired through donation. Further, in case a spouse of the taxpayer whose period of marriage with the taxpayer is twenty years or more has acquired real estate for his/her own use or appropriated donated money to acquire a residence for his/her own use a exemption for spouse of ¥20 million or less is allowed. No property used for public interest is subject to taxation. In a case where property is donated by a corporation, the property is not subject to gift tax but to income tax.</p>
<p>Land Value Tax: Land Value Tax Law</p>	<p>Individuals and corporations who are owners of land in Japan. (This tax was suspended after 1998 for the time being).</p>	<p>Total amount of the assessment value (the assessed value for the inheritance tax) of all the land held by a taxpayer as of the first day of each year, minus the amount of the basic deduction.</p>
<p>Consumption Tax: Consumption Tax Law</p>	<p>Enterprises and those who receive deliveries of foreign goods from bonded areas.</p>	<p>(1) Domestic transactions: sales price of assets</p> <p>(2) Import transactions: delivery price (including customs duty and other selective consumption taxes) of imported goods.</p>

the National Tax System

Rate	Report & Payment												
<p>(2) Deduction for dependent ¥60,000 x (20 minus age of the dependent)</p> <p>(3) Deduction for handicapped person ¥60,000 (¥120,000 in case seriously handicapped) x (70 minus age of the handicapped person)</p>													
<p>(1) At the time of donation (Tax Rate): 20% evenly</p> <p>(2) At the time of inheritance (Tax Rate): Same as the rate of inheritance tax (Tax Deduction)</p> <p>* The same as the case of inheritance tax</p> <p>* The tax amount already paid shall be deducted from the amount of inheritance tax (the remaining part shall be returned).</p>	<p>(Applicable Procedures)</p> <p>* A notice to the effect that this system is applied shall be submitted as an attachment during the period from February 1 to March 15 of the year next to the year of inheritance.</p> <p>* In case the above notice is submitted at the time of the initial donation, this system may be applicable till the time of inheritance.</p> <p>* Brothers and sisters as donees may select separately for each father and mother as a specified donor.</p>												
<table> <tr> <td>¥ 2 million or less</td><td>10%</td></tr> <tr> <td>¥ 3 million or less</td><td>15%</td></tr> <tr> <td>¥ 4 million or less</td><td>20%</td></tr> <tr> <td>¥ 6 million or less</td><td>30%</td></tr> <tr> <td>¥10 million or less</td><td>40%</td></tr> <tr> <td>More than ¥10 million</td><td>50%</td></tr> </table>	¥ 2 million or less	10%	¥ 3 million or less	15%	¥ 4 million or less	20%	¥ 6 million or less	30%	¥10 million or less	40%	More than ¥10 million	50%	<p>(1) Tax payment by self-assessment</p> <p>(2) Time limit for tax payment: The person to pay tax on the property acquired through donation shall submit a declaration and pay tax during the period from February 1 to March 15 of the next year.</p>
¥ 2 million or less	10%												
¥ 3 million or less	15%												
¥ 4 million or less	20%												
¥ 6 million or less	30%												
¥10 million or less	40%												
More than ¥10 million	50%												
0.3%	<p>Self-assessment</p> <p>Taxpayers should file returns between 1 October and 31 October every year and pay the tax amount separately on that day and on another day no later than 31 March of the next year.</p>												
4%	<p>Self-assessment</p> <p>(1) Domestic transactions</p> <p>An enterprise must file a tax return and pay taxes due within 2 months of the day following the last day of the tax period.</p>												

Appendix II Summary of

Tax	Taxpayer	Tax Base
Liquor Tax: Liquor Tax Law	Liquor manufacturer or person who withdraws liquor from a bonded area.	Quantity of liquor
Tobacco Tax: Tobacco Tax Law	Manufacturer of tobacco products (including cigarettes, cigars, and other tobacco products) or person who withdraws tobacco products from bonded areas.	Specific duty: quantity for cigarettes and weight for other products.
Special Tobacco Tax: The law concerning special measures for securing	The same in the case of Tobacco Tax	The same as in the case of the Tobacco Tax

the National Tax System

Rate	Report & Payment
	(2) A tax return must be filed and taxes must be paid by the time of receipt of taxable goods from bonded areas. The payment can be deferred up to 3 months if collateral is offered.
<p>Rates depending upon kind, class, and alcoholic content (per kilolitre)</p> <ol style="list-style-type: none"> Sparkling Alcohol Drinks (beer etc.) <ul style="list-style-type: none"> ¥220,000 Low malt beer (the ratio of malt not less than 25% and less than 50%, and 10% of alcohol) ¥178,125 Low malt beer (the ratio of malt less than 25%, and 10% of alcohol) ¥134,250 Others (non hop-based) ¥80,000 Fermented Liquor ¥140,000 <ul style="list-style-type: none"> Refined <i>Sake</i> ¥120,000 Wine ¥80,000 <i>Shochu</i> etc. (20%) ¥200,000 (additional ¥10,000 per 1%) <ul style="list-style-type: none"> Whisky, Brandy, Spirits (37%) ¥370,000 (additional ¥10,000 per 1%) Miscellaneous liquor (20%) ¥220,000 (additional ¥11,000 per 1%) <ul style="list-style-type: none"> <i>Sake</i> compound ¥100,000 <i>Mirin</i> ¥20,000 Sweet wine or Liqueur (12%) ¥120,000 (additional ¥10,000 per 1%) Powdered Liquor ¥390,000 	<p>With respect to liquor shipped from manufacturing premises, a return must be filed by the end of the next month following shipment and the tax must be paid by the end of the month after next.</p> <p>With respect to liquor withdrawn from bonded areas, a return must be filed before withdrawal and tax paid at the time of withdrawal. However, when a business enterprise files a special return on tariff with the Custom-House, the enterprise shall pay the taxes to the Custom-House by the end of the following month of the day that the enterprise files a return and takes goods out of the bonded area.</p> <p>If security is offered, payment may be postponed for 1 month.</p>
Unit tax: 3,552 yen per one thousand pieces	<p>A tax return must be filed and taxes must be paid by the manufacturer, by the end of the next month following shipment or by importer, by the time of withdrawal from a bonded area. However, when the manufacturer or importer files a special return on tariff with the Custom-House, the enterprise shall pay the taxes to the Custom-House by the end of the following month of the day that the enterprise files a return and takes goods out of the bonded area.</p> <p>If security is offered, payment may be postponed for up to one month for a manufacturer and two months (one month for an individual who files a special return on tariff) for an importer.</p>
Unit tax: 820 yen per one thousand pieces	Taxpayers must declare and pay the tax upon declaring the Tobacco Tax.

Appendix II Summary of

Tax	Taxpayer	Tax Base
finances to succeed debt in the General Account		
Gasoline Tax: Gasoline Tax Law	Person who ships from a refinery or person who withdraws gasoline from bonded areas	Quantity of gasoline shipped from a refinery or withdrawn from a bonded area minus 1.35% as an deduction for losses
Aviation Fuel Tax: Aviation Fuel Tax Law	Owners of aircraft in principle, or users of aircraft	Quantity of aviation fuel loaded on aircraft
Liquefied Petroleum Gas Tax Liquefied Petroleum Gas Tax Law	Person who puts liquefied petroleum gas into an automobile or withdraws taxable liquified petroleum gas from bonded areas	Weight of taxable gas shipped from a filling station or withdrawn from bonded areas
Stamp Tax: Stamp Tax Law	Person who drafts documents taxable	Number of copies of taxable documents
Registration and License Tax: Registration and License Tax Law	Applicant for the registration of creation, transfer, alteration or lapse of the right on property (including intangible property) and for the license for a physician, lawyer, etc.	Value of the real property, amount of capital and number of copyrights, etc.
Motor Vehicle Tonnage Tax: Motor Vehicle Tonnage Tax Law	Users of motor vehicles who obtain a motor vehicle inspection certificate, or users of light motor vehicles who obtain a vehicle number.	Number of motor vehicles

the National Tax System

Rate	Report & Payment
¥48,600 per kilolitre (from 1 December 1993 to 31 March 2008)	By the refiner, by the end of the following month, or by the person making the withdrawal, at the time of withdrawal. However, when a business enterprise files a special return on tariff with the Custom-House, the enterprise shall pay the taxes to the Custom-House by the end of the following month of the day that the enterprise files a return and takes goods out of the bonded area. If security is offered, payment may be postponed for up to 2 months (or 3 months in the case of withdrawal).
¥26,000 per kilolitre	Taxpayers must file a return and pay the tax by the end of the month following the month in which the fuel was loaded on their aircraft.
¥17.5 per kilogram	Return: by the end of the following month Payment: by the end of the second next month With respect to a person making a withdrawal, at the time of withdrawal. However, when a business enterprise files a special return on tariff with the Custom-House, the enterprise shall pay the taxes to the Custom-House by the end of the following month of the day that the enterprise files a return and takes goods out of the bonded area. If security is offered payment may be postponed for 1 month.
Varying rates according to types of documents, from ¥200 (minimum) to ¥600,000 (maximum)	By affixing stamps on deeds, etc., and invalidating stamps by signature.
For example; Value of Real property0.1%~2% Capital 0.7% Copyright ¥18,000 per case	The tax is paid with revenue stamps at the time of registration.
Varying rates according to types, weights and valid period of inspection certificate of motor vehicles.	By affixing stamps on designated documents by the time of obtaining a motor vehicle inspection certificate or designation of vehicle number

Appendix II Summary of

Tax	Taxpayer	Tax Base
Local Road Tax; Local Road Tax Low	Same as for the Gasoline Tax	Same as for the Gasoline Tax
Promotion of Power-Re-sources Development Tax; Promotion of Power-Re-sources Development Tax Law	Ordinary electric utility enterprises	Quantity of electricity for sale (1) Electricity that ordinary electric utility enterprises supply to others in compliance with demand (2) Electricity that ordinary electric utility enterprises consume themselves (excluding that which they consume directly for generation of electricity)
Petroleum and Coal Tax; Petroleum and Coal Tax Law	Those who ship crude petroleum, gaseous hydrocarbons or coal from extracting stations or those who withdraw crude petroleum, petroleum products, gaseous hydrocarbons or coal from bonded areas.	Quantity of crude petroleum, imported petroleum products, or gaseous hydrocarbons or coal.

the National Tax System

Rate			Report & Payment
¥5,200 per kilolitre (from 1 December 1993 to 31 March 2003)			By manufacturer or importer together with the Gasoline Tax
per 1,000 kilowatt-hours			Return—stating the following: (1) amount of electricity sold (2) amount of electricity consumed by the electric utility enterprise itself (3) Payment—by the end of the following month
	From april 1, 2005	From april 1, 2007	
	¥400	¥375	
	From April 1,2005	From April 1,2007	<p>A return shall be filed and the tax shall be paid by the end of the following month when shipment is made. A person who intends to withdraw goods shall file a return and pay the tax when the person withdraws the goods from the bonded area.</p> <p>However, when a person intends to file a special return on tariffs, the person shall file such a return and pay the tax by the end of the following month when the person withdraws goods.</p> <p>A person approved by the Commissioner of the NTA shall file a return and pay the tax by the end of the following month when the person withdraws.</p>
Crude petroleum or imported petroleum products;(per kl;)	¥2,040	¥2,040	
Natural gas (per tone)	¥960	¥1,080	
Gaseous hydrocarbons (except natural gas) (per tone)	¥940	¥1,080	
Coal (per tone)	¥460	¥700	

Appendix III Summary of

Tax	Taxpayer	Tax Base
<p>A Prefectural Taxes</p> <p>1. Prefectural Inhabitants Tax</p>	<p>(1) Individual with address in the prefecture</p> <p>(2) Individuals with an office, working place, or house, but not a domicile</p> <p>(3) Corporations with an office or working place in prefectures</p> <p>(4) Corporations with dormitories, etc. but not an office or working place in prefectures</p> <p>(5) Associations or foundations other than juridical persons having their offices, business places or dormitories in prefectures and those who have a representative or manager</p> <p>(6) The following individuals are exempted from tax:</p> <p>(a) Individuals who are levied only per capita inhabitants tax, and total income in the previous year is under the amount stipulated in local ordinance in accordance with certain standard.</p> <p>(b) Individuals receiving livelihood assistance grants under the Life Aid Laws</p> <p>(c) Physically disabled, widows, and individuals under 20 (except those whose income in the previous year was over ¥1,250,000)</p>	<p>(1) Individuals</p> <p>(a) per capita</p> <p>(b) the total income* of the previous year (applies only to taxpayer (1))</p> <p>*Retirement income, timber income, capital gains from the transfer of land or buildings, capital gains from the transfer of stocks, and miscellaneous income from futures transactions are taxed separately from other incomes during the taxable years</p> <p>Exemptions</p> <p>(i) casualty losses</p> <p>(ii) deduction for medical expenses</p> <p>(iii) deduction for social insurance premiums</p> <p>(iv) deduction for small-scale enterprise mutual aid premiums</p> <p>(v) deduction for life insurance premiums</p> <p>(vi) deduction for fire and other casualty insurance premiums</p> <p>(vii) deduction for the handicapped: ¥260,000 (for severely handicapped person, ¥300,000)</p> <p>(viii) exemption for widows or working</p> <p>For certain widows: ¥300,000, students: ¥260,000</p> <p>(ix) exemption for spouses: ¥330,000 (for spouses over 70 years old: ¥380,000)</p> <p>(x) special exemption for spouses: ¥330,000</p> <p>(xi) exemption for dependents: ¥330,000 for each, deduction for elderly dependents: ¥380,000 for each, exemption for dependents who are from 16 to 22 years old: ¥430,000 for each</p> <p>(xii) basic exemption: ¥330,000</p> <p>(xiii) when taxable income is less than the amount of $¥350,000 \times (1 + \text{number of dependents including spouse}) + ¥320,000$, such a person is exempt from taxation.</p> <p>(2) Corporations, etc.</p> <p>(a) per corporation</p> <p>(b) on corporation tax (applies only to taxpayer (3))</p>

the Local Tax System

Rate	Report & Payment
<p>(1) Individuals</p> <p>(a) per capita: ¥1,000 (standard)</p> <p>(b) on total income</p> <p>Rates: on total taxable income</p> <p>Not over ¥7,000,000 2%</p> <p>Over ¥7,000,000 3%</p> <p>(uniformly 4% after FY2007)</p> <p>Tax credit for dividends received if taxable income, including dividends, is</p> <p>(i) not over ¥10,000,000; 0.8% of the dividends received</p> <p>(ii) over ¥10,000,000; 0.4% of the dividends received</p> <p>(1.2% and 0.6% after FY2007)</p> <p>(2) Corporations</p> <p>(a) per corporation</p> <p>(i) Corporations with capital plus reserve funds of more than ¥5 billion Standard ¥800,000</p> <p>(ii) Corporations with capital plus reserve fund of more than ¥1 billion but not more than ¥5 billion ¥540,000</p> <p>(iii) Corporations with capital plus reserve funds of more than ¥100 million yen but not more than 1 billion ¥130,000</p> <p>(iv) Corporations with capital plus reserve funds of more than ¥10 million but not more than ¥100 million ¥50,000</p> <p>(v) Other corporations ¥20,000</p> <p>(b) on corporation tax:</p> <p>5.0% (standard)</p> <p>6.0% (maximum)</p>	<p>(1) Individuals</p> <p>Taxpayers (1) and (2)</p> <p>(a) Assessed by municipality together with the Municipal Inhabitants Tax</p> <p>(b) Collected in June, August, October and January (standard) or withheld from June to May at source by an employer for employment income earners</p> <p>(2) Corporations</p> <p>Taxpayers(3), (4) and (5)</p> <p>Self-assessed within generally 2 months of the end of the accounting period</p>

Appendix III Summary of

Tax	Taxpayer	Tax Base
Separate taxation of capital gains		
	Individuals	<p>(1) Long-term capital gains, etc. (capital gains from land or buildings continuously owned for more than 5 years as of 1 January of the year in which the transfer took place)</p> <p>(2) Short-term capital gains (capital gains from land or buildings which have been held no longer than 5 years as of 1 January of the year in which the transfer took place)</p> <p>(3) Capital gains from transfer of stocks</p> <p>(4) Miscellaneous incomes from futures transactions</p>
2. Enterprise Tax	(1) Corporations	<p>(1) Corporations: Net income liquidation income or gross proceeds for each accounting period</p> <p>For corporations (excluding specified corporations) whose capital is in excess of ¥100 million, the total of the income levy, added-value levy and capital levy is calculated as follows:</p> <p>Income levy: Income</p> <p>Added-value levy:</p> <p>The amounts of added value (Compensations/wages + net interest paid + net rents paid ± profits and losses of a single fiscal year)</p> <p>* In case the amounts of compensations/wages exceed 70% of distributed profits (compensations/wages + net interest paid + net rents paid), the amount in excess (employment security deduction) shall be deducted from the amount of the distributed profits</p> <p>Capital levy:</p> <p>The amount of capital (amount of capital or investment + capital reserve fund or consolidated capital reserve fund)</p>

the Local Tax System

Rate	Report & Payment
from the transfer of land, buildings or stocks	
<p>(1) Long-term capital gains Deductions: An increased deduction varying from ¥8 million to ¥50 million is available according to the type of transfer and assets</p> <p>Tax rate: 1.6% (2.0%) of taxable long-term capital gains</p> <p>(2) Short-term capital gains Deductions: Special deduction varying from ¥8 million to ¥50 million is available according to the type of transfer and assets Tax amount: 3.0% (3.6%) of the taxable short-term capital gains.</p> <p>(3) 1.6% (2.0%) (1% (1.2%) from 2004 to 2008 for listed stocks)</p> <p>(4) 1.6% (2.0%)</p> <p>Note) The figures in parenthesis are tax rates applied after FY2007.</p>	<p>(1) Assessed by municipalities together with the Municipal Inhabitants Tax</p> <p>(2) Collected in June, August, October, and January</p>
<p>(1) Corporations:</p> <p>(a) Electricity suppliers, gas suppliers, life insurance, and casualty insurance businesses: 1.3% (maximum 1.43%) on gross proceeds</p> <p>(b) Other businesses</p> <p>(i) Special corporations: 5% (maximum 5.5%) on annual net income of under ¥4,000,000, and 6.6% (maximum 7.26%) on annual income of more than ¥4,000,000 or liquidation income</p> <p>(ii) Other corporations: 5% (maximum 5.5%) on annual net income of ¥4,000,000 or less 7.3% (maximum 8.03%) on annual net income of more than ¥4,000,000, and 9.6% (maximum 10.56%) on annual net income of more than ¥8,000,000 or liquidation income The flat rate of 9.6% or 6.6% is applicable to corporations capitalized at more than ¥10,000,000 and with offices and branches in more than 3 prefectures.</p> <p>(c) Corporations whose capital is in excess of ¥100 million Income levy 3.8% for incomes of ¥4 million or less 5.5% for the incomes of ¥4 million to ¥8</p>	<p>(1) Corporations: Self-assessed generally within 2 months of the end of the accounting period.</p>

Appendix III Summary of

Tax	Taxpayer	Tax Base
	(2) Individual operating type I, II, or III business	<p>* For certain holding companies, the amount calculated by multiplying the capital by the rate of booked values of the stocks of its subsidiaries shall be deducted from the capital amount.</p> <p>* The amount in excess of ¥100 billion out of the entire capital shall be compressed step by step.</p> <p>(2) Individuals: Net income for the preceding calendar year Income is computed in the same way as national income tax. In computing taxable income, a deduction for proprietors of ¥2,900,000 is allowed.</p>
3. Local Consumption Tax	Enterprises and those who receive deliveries of foreign goods from bonded areas	<p>(1) Domestic transactions: amount of Consumption Tax</p> <p>(2) Import transactions: amount of Consumption cargoes from bonded areas</p>
4. Real Property Acquisition Tax	Person acquiring real property	<p>Value of real property at the time of acquisition (minimum exemption: ¥100,000 for acquisition of land, ¥230,000 for newly constructed buildings and ¥120,000 for other buildings.</p> <p>Special deduction of ¥12,000,000 from the tax basis is allowed for acquisition of eligible new or old houses.</p> <p>The tax levied on the appraised acquisition value of the site of these houses is reduced by a certain amount</p>

the Local Tax System

Rate	Report & Payment
<p>million or liquidation incomes Added value levy 0.48%; Capital levy 0.2% The tax rate of 7.2% shall be applied evenly to various levies or corporations having their offices or business places in three or more prefectures</p> <p>(2) Individuals: Category I 5% (standard) 5.5% (maximum) Category II 4% (standard) 4.4% (maximum) Category III 5% (standard) 5.5% (maximum) Category III 3% (standard) (certain category) 3.3% (maximum)</p>	<p>(2) Individuals: Assessed by prefecture: collected in August and November based on the self statement submitted by 15 March.</p>
<p>25% (equivalent to 1% of consumption tax rate)</p>	<p>Self-assessment</p> <p>(1) The enterprises who are subject to file a final return must file a final return with that of Consumption Tax and pay the declared Local Consumption Tax amount with the Consumption Tax amount by the deadline of declaration of the Consumption Tax.</p> <p>(2) Those who receive taxable cargoes from bonded areas must file a fixed return with that of Consumption Tax to the Director-General of Customs and pay the declared Local Consumption Tax amount with the Consumption Tax amount.</p> <p>[Note1] The enterprises declare and pay Local Consumption Tax with the same return and tax payment slip at the same time as Consumption Tax.</p> <p>[Note2] While Local Consumption Tax is a Prefectural Tax, the State executes this tax with Consumption Tax for the time being given the burden on taxpayers, etc.</p>
<p>4% (standard) Note) 3% for the houses and lands acquired between April 1, 2006 and March 31, 2009. 3.5% for the buildings other than house acquired between April 1, 2006 and March 31, 2008.)</p>	<p>Assessed and collected by prefecture</p>

Appendix III Summary of

Tax	Taxpayer	Tax Base
5. Prefectural Tobacco Tax	Manufacturer, wholesaler, and importer of tobacco products	Specific duty: quantity of the tobacco product sold in the prefecture
6. Golf Course Utilisation Tax	Persons who use golf courses	–
7. Automobile Tax	Owner of automobiles	

the Local Tax System

Rate	Report & Payment
¥1,074 per thousand cigarettes	Self-assessment Payment by the end of the following month
Standard: ¥800 per day, per player Maximum: ¥1,200	Collected specially with the use rate by Golf course administrators. Payment by a time limit.
Standard: (1) Passenger car (a) Car with a cylinder volume in excess of 2,000 cc Over But not over (Standard) 2,500cc Commercial ¥ 13,800 Non-commercial ¥ 45,000 2,500cc – 3,000cc Commercial ¥ 15,700 Non-commercial ¥ 51,000 3,000cc – 3,500cc Commercial ¥ 17,900 Non-commercial ¥ 58,000 3,500cc – 4,000cc Commercial ¥ 20,500 Non-commercial ¥ 66,500 4,000cc – 4,500cc Commercial ¥ 23,600 Non-commercial ¥ 76,500 4,500cc – 6,000cc Commercial ¥ 27,200 Non-commercial ¥ 88,000 6,000cc Commercial ¥ 40,700 Non-commercial ¥ 111,000 (b) Small 4 wheel car with cylinder volume of: Over But not over (Standard) 1,000cc Commercial ¥ 7,500 Non-commercial ¥ 29,500 1,000cc – 1,500cc Commercial ¥ 8,500 Non-commercial ¥ 34,500 1,500cc – 2,000cc Commercial ¥ 9,500 Non-commercial ¥ 39,500 (2) Truck (Tax base for trucks whose loading capacity is over 4 tonne and not more than 5 tonne.) (Standard) Commercial ¥ 18,500 Non-commercial ¥ 25,000 (3) Bus (Tax base for buses whose riding capacity is over 40 and not more than 50 passengers.) Commercial use: (Standard) For ordinary passengers ¥ 17,500 Others ¥ 38,000 Non-commercial use ¥ 49,000 (4) Three-wheeled small car (Standard) Commercial ¥ 4,500 Non-commercial ¥ 6,000	The owner of the car is assessed on 1 April by prefecture: collected in May In case that buying a car newly, collected in registration.

Appendix III Summary of

Tax	Taxpayer	Tax Base
8. Automobile Acquisition Tax	Person acquiring an automobile	Value of automobile at the time of acquisition (minimum exemption: ¥500,000 to 31 March 2008)
9. Mine lot Tax	Owner of mining rights	Mine-lot area
10. Hunting Tax	Registered hunters	
11. Light-oil Delivery Tax	The persons who withdraw light oil from a source of supply or specially agreed traders	Quantity of light-oil purchased
B. Municipal 1. Municipal Inhabitants Tax	<p>(1) Individuals with a domicile within a municipality</p> <p>(2) Individuals with an office, working place, or house but not having a domicile</p> <p>(3) Corporations with an office or working place</p> <p>(4) Corporations with dormitories, etc., but not an office nor working place</p> <p>(5) Associations or foundations other than juridical persons having their offices, business places or dormitories in prefectures and those who have a representative or manager</p> <p>(6) The following individuals are exempted from tax :</p> <p>(a) Individuals who are levied only per capita inhabitants tax, and total income in the previous year is under the amount stipulated in local ordinance in accordance with certain standard.</p> <p>(b) Individuals receiving livelihood assistance grants under the Social Aid Laws</p> <p>(c) Physically disabled, widows, individuals aged under 20 (except those whose income in the previous year was over 1,250,000 yen)</p>	<p>(1) Individuals</p> <p>(a) per capita</p> <p>(b) on income (applies only to taxpayer (1)) the same tax base as that of the prefectural inhabitants tax</p> <p>(2) Corporations</p> <p>(a) per capita</p> <p>(b) on corporation tax (applies only to taxpayer(3))</p>

the Local Tax System

Rate	Report & Payment																																							
Motor vehicle for non-commercial use (except a light motor vehicle).....5% Motor vehicle for commercial use (except a light motor vehicle)3% Light motor vehicle 3%	Self-assessment by the following date. (1) In case submitting new registration or new report of using :the date of registration (2) In case should register removal: the date within 15 days in removal. (3) Others: the date within 15 days in acquisition. In conducting self-assessment, a taxpayer submits the declaration with a stamp and pay taxes.																																							
(1) Prospecting lot: ¥200 per hectare (2) Working lot: ¥400 per hectare (3) Placer lot: ¥200 per hectare	Assessed by the prefecture: collected in May																																							
¥16,500, ¥11,000, ¥5,500 depending on the kind of license	Assessed and collected by the prefecture according to the regulations.																																							
¥32,100 per kilolitre from 1 December 1993 to 31 March 2008)	Collected by wholesaler and self-assessed by the end of the next month.																																							
(1) Per capita (a) Individual ¥3,000 (Standard rate) (b) Corporation	(1) Taxpayers (1) and (2) (a) Assessed by municipality (b) Collected in June, August, October and January (standard) or withheld at source every month by employers from June to May for employment income earners (2) Taxpayers (3), (4) and (5) Generally Self-assessed within 2 months after the end of an accounting period																																							
<table><tr><th>Capital plus Reserve Fund</th><th>Employees</th><th>Standard</th><th>Maximum</th></tr><tr><td rowspan="2">more than ¥ 5 billion</td><td>more than 50</td><td>¥ 3,000,000</td><td>¥ 3,600,000</td></tr><tr><td>50 or less</td><td>¥ 410,000</td><td>¥ 492,000</td></tr><tr><td rowspan="2">more than ¥1 billion but not more than ¥5 billion</td><td>more than 50</td><td>¥ 1,750,000</td><td>¥ 2,100,000</td></tr><tr><td>50 or less</td><td>¥ 410,000</td><td>¥ 492,000</td></tr><tr><td rowspan="2">more than ¥100 million but no more than ¥1 billion</td><td>more than 50</td><td>¥ 400,000</td><td>¥ 480,000</td></tr><tr><td>50 or less</td><td>¥ 160,000</td><td>¥ 192,000</td></tr><tr><td rowspan="2">more than ¥10 million but no more than ¥100 million</td><td>more than 50</td><td>¥ 150,000</td><td>¥ 180,000</td></tr><tr><td>50 or less</td><td>¥ 130,000</td><td>¥ 156,000</td></tr><tr><td rowspan="2">no more than ¥10 million</td><td>more than 50</td><td>¥ 120,000</td><td>¥ 144,000</td></tr><tr><td>50 or less</td><td>¥ 50,000</td><td>¥ 60,000</td></tr></table>	Capital plus Reserve Fund	Employees	Standard	Maximum	more than ¥ 5 billion	more than 50	¥ 3,000,000	¥ 3,600,000	50 or less	¥ 410,000	¥ 492,000	more than ¥1 billion but not more than ¥5 billion	more than 50	¥ 1,750,000	¥ 2,100,000	50 or less	¥ 410,000	¥ 492,000	more than ¥100 million but no more than ¥1 billion	more than 50	¥ 400,000	¥ 480,000	50 or less	¥ 160,000	¥ 192,000	more than ¥10 million but no more than ¥100 million	more than 50	¥ 150,000	¥ 180,000	50 or less	¥ 130,000	¥ 156,000	no more than ¥10 million	more than 50	¥ 120,000	¥ 144,000	50 or less	¥ 50,000	¥ 60,000	
Capital plus Reserve Fund	Employees	Standard	Maximum																																					
more than ¥ 5 billion	more than 50	¥ 3,000,000	¥ 3,600,000																																					
	50 or less	¥ 410,000	¥ 492,000																																					
more than ¥1 billion but not more than ¥5 billion	more than 50	¥ 1,750,000	¥ 2,100,000																																					
	50 or less	¥ 410,000	¥ 492,000																																					
more than ¥100 million but no more than ¥1 billion	more than 50	¥ 400,000	¥ 480,000																																					
	50 or less	¥ 160,000	¥ 192,000																																					
more than ¥10 million but no more than ¥100 million	more than 50	¥ 150,000	¥ 180,000																																					
	50 or less	¥ 130,000	¥ 156,000																																					
no more than ¥10 million	more than 50	¥ 120,000	¥ 144,000																																					
	50 or less	¥ 50,000	¥ 60,000																																					

Appendix III Summary of

Tax	Taxpayer	Tax Base
	Separate taxation of capital gains	
	Individuals	<p>(1) Long-term capital gains (capital gains from land or buildings continuously owned for more than 5 years as of 1 January of the year in which the transfer took place) of the previous year</p> <p>(2) Short-term capital gains of the previous year (capital gains not categorized as long term capital gains defined above)</p> <p>(3) Capital gains from transfer of stocks, etc.</p> <p>(4) Miscellaneous income from transactions of futures</p>
2. Property Tax	Owner of land, buildings, or depreciable business assets (except for vehicles)	Market value of the property registered in the property tax cadastre (Minimum exemption: ¥300,000 for land, ¥200,000 for house and ¥1,500,000 for depreciable assets)
3. Light Vehicle Tax	Owners of light vehicles	

the Local Tax System

Rate	Report & Payment										
<p>(2) On total taxable income</p> <p>Rates (Standard): (income rate)</p> <table><tr><td>Not over</td><td>¥2,000,000</td><td>3%</td></tr><tr><td></td><td>¥7,000,000</td><td>8%</td></tr><tr><td>Over</td><td>¥7,000,000</td><td>10%</td></tr></table> <p>uniformly 6% after FY2007</p> <p>Tax credit for dividends received if taxable income, including dividends, is</p> <p>(i) not over ¥10,000,000; 2.0% of the dividends received</p> <p>(ii) over ¥10,000,000; 1.0% of the dividends received</p> <p>(1.6% and 0.8% after FY2007)</p> <p>(3) On corporation tax: 12.3%(standard), 14.7%(maximum rate)</p>	Not over	¥2,000,000	3%		¥7,000,000	8%	Over	¥7,000,000	10%		
Not over	¥2,000,000	3%									
	¥7,000,000	8%									
Over	¥7,000,000	10%									
from the transfer of land or buildings etc.											
<p>(1) Long-term capital gains</p> <p>Deductions: same as for the prefectural inhabitants tax</p> <p>Tax amount: 3.4% (3.0%) of taxable long-term capital gains</p> <p>(2) Short-term capital gains</p> <p>Tax amount: 6% (5.4%) of the taxable short-term capital gain</p> <p>(3) 3.4% (3.0%) (2% (1.8%) from 2004 to 2008 for listed stocks)</p> <p>(4) 3.4% (3.0%)</p> <p>Note) The figures in parenthesis are tax rates applied after FY2007.</p>											
1.4% (standard)	Assessed by municipality: collected in April, July, December, and February										
<p>(1) Small size Two-wheeled vehicles: ¥4,000</p> <p>(2) Light vehicles and small size special vehicles</p> <table><tr><td>(a) with 2 wheels:</td><td>¥2,400</td></tr><tr><td>(b) with 3 wheels:</td><td>¥3,100</td></tr><tr><td>(c) with 4 wheels or over</td><td></td></tr></table> <p>passenger cars:</p> <table><tr><td>commercial use</td><td>¥5,500</td></tr><tr><td>non-commercial use</td><td>¥7,200</td></tr></table> <p>trucks:</p>	(a) with 2 wheels:	¥2,400	(b) with 3 wheels:	¥3,100	(c) with 4 wheels or over		commercial use	¥5,500	non-commercial use	¥7,200	Assessed to the owner of the light car as of April 1 by municipality: Collected in April
(a) with 2 wheels:	¥2,400										
(b) with 3 wheels:	¥3,100										
(c) with 4 wheels or over											
commercial use	¥5,500										
non-commercial use	¥7,200										

Appendix III Summary of

Tax	Taxpayer	Tax Base
4. Minicipal Tobacco Tax	Manufacturers, wholesaler, and importers of tobacco products	Specific duty: quantity of the tobacco product sold in the prefecture
5. Mineral Product Tax	Mine operators	Value of mineral products mined
6. Special Land holding Tax	<p>(1)(a) Special land holding tax on holding: Owner of the land as of 1 January every year</p> <p>(b) Special land holding tax on acquisition: Person who acquires the land within a year before 1 January (or 1 July)</p> <p>(2) Non-taxable case The following land is not subject to the tax:</p> <p>(a) Land acquired by, or under the ownership of, State or local public entities</p> <p>(b) Land acquired by corporate merger or inheritance</p> <p>(c) Land used, in accordance with specified state or local public entity policy for decentralization of factories, etc.</p>	Value of land paid when it is acquired (Minimum exemption: In cases where the area of land owned or acquired is smaller than the prescribed area (2,000 sq. m. to 10,000 sq. m.) in accordance with the classification of municipalities, the tax is exempt)
7. Bathing Tax	Persons bathing in hot springs	
8. Urban Planning Tax	Owners of houses and land located in areas where urban planning schemes are enforced	Same as the Property Tax with respect to buildings and land
9. Business Office Tax	Person conducting business	<p>(1) Floor space</p> <p>(2) Wages</p>

Note: 1. Prefectural government has right to impose Water and Land Utilization Tax to finance the
2. Municipal government has rights to impose Water and Land Utilization Tax, Public Facilities Tax, Land
3. Prefectural and municipal government can impose other taxes (General Tax and Object Tax which is

the Local Tax System

Rate	Report & Payment
commercial use ¥3,000 non-commercial use ¥4,000 (3) Motorcycle: ¥2,500, ¥1,600, ¥1,200 or ¥1,000 (according to cylinder volume)	
¥3,298 per thousand cigarettes	Self-assessment Payment by the end of the following month
1% (standard), 1.2% (maximum); 0.7% (standard), 0.9% (maximum) for mines whose products are under ¥2,000,000 in a month	Self-assessment by the end of the next month.
Special landholding tax on holdings; 1.4% Special landholding tax on acquisition; 3.0% The property tax or the real property acquisition tax on the land concerned is creditable.	Self-assessed by the end of May of the year concerned (special landholding tax on holdings) or by the end of February or of August of the year concerned (special landholding tax on acquisitions)
¥150 yen per day	Collected specially by operators of mineral baths
0.3% (maximum)	Assessed and paid together with Property Tax
(1) ¥600 per one square meter (2) 0.25%	Individuals: Self-assessed no later than 15 March of the following year Corporations: Self-assessed within two months after the close of an accounting period

administration cost which is stipulated in law.

Development Tax and National Health Insurance Tax to finance the administration cost which is stipulated in law. not stipulated in the Local Tax Law) with the consent of the Ministry of Internal Affairs and Communications.

Appendix III Summary of

Appendix IV INCOME TAX BURDEN

1. Income Tax Revenue

(In 100 million yen)

Fiscal Year	Total National Tax Revenue (A)	Income Tax Revenue (B)	B/A
1950	5,702	2,201	38.6
1955	9,364	2,787	29.8
1960	18,010	3,906	21.7
1965	32,785	9,704	29.6
1970	77,732	24,282	31.2
1975	145,043	54,823	37.8
1980	283,688	107,996	38.1
1985	391,502	154,350	39.4
1986	428,510	168,267	39.3
1987	478,068	174,371	36.5
1988	521,938	179,538	34.4
1989	571,361	213,815	37.4
1990	627,798	259,955	41.4
1991	632,110	267,493	42.3
1992	573,964	232,314	40.5
1993	571,142	236,865	41.5
1994	540,007	204,175	37.8
1995	549,630	195,150	35.5
1996	552,261	189,649	34.3
1997	556,007	191,827	34.5
1998	511,977	169,961	33.2
1999	492,139	154,468	31.4
2000	527,209	187,889	35.6
2001	499,684	178,065	35.6
2002	458,442	148,122	32.3
2003	453,694	139,146	30.7
2004	481,029	150,954	31.4
2005	522,905	167,018	31.9
2006(Budget)	509,243	157,974	31.0

Notes : For the figures before 1985, total national tax revenue includes the profits from the government tobacco monopoly and other sources.

2. Burden of Income Tax and Local Inhabitants Taxes

(In 100 million yen)

Fiscal Year	National Income (A)	Income Tax (B)	Local Inhabitants Taxes	Total (C)	B/A	C/A	Ratio of (C) to Total Tax Revenue
1950	33,815	2,201	464	2,665	6.5%	7.9%	35.1
1955	69,733	2,787	715	3,502	4.0	5.0	26.6
1960	134,967	3,906	996	4,902	2.9	3.6	19.3
1965	268,270	9,704	3,429	13,133	3.6	4.9	27.2
1970	610,297	24,282	6,969	31,251	4.0	5.1	27.1
1975	1,239,907	54,823	20,989	75,812	4.4	6.1	33.5
1980	2,032,410	107,996	43,046	151,042	5.4	7.6	34.1
1985	2,610,890	154,350	66,030	220,380	5.9	8.5	35.3
1990	3,483,454	259,955	105,557	365,512	7.4	10.4	38.0
1991	3,710,808	267,493	112,559	380,052	7.2	10.2	38.7
1992	3,693,236	232,314	115,332	347,646	6.3	9.4	37.8
1993	3,690,327	236,865	113,691	350,556	6.4	9.4	38.6
1994	3,740,795	204,175	99,805	303,980	5.4	8.1	35.1
1995	3,742,775	195,151	101,872	297,023	5.2	7.9	33.5
1996	3,791,109	189,649	95,549	285,198	5.0	7.5	31.6
1997	3,827,685	191,827	104,275	269,102	5.0	7.0	29.3
1998	3,725,089	169,961	93,183	263,144	4.6	7.1	30.2
1999	3,667,446	154,468	91,490	245,958	4.2	6.7	29.2
2000	3,715,901	187,889	97,202	285,091	5.1	7.7	32.3
2001	3,609,408	178,065	95,419	273,484	4.9	7.6	32.0
2002	3,557,905	148,112	86,159	234,271	4.2	6.7	29.6

2003	3,584,259	139,146	81,302	220,448	3.9	6.2	28.2
2004	3,610,471	150,954	80,018	230,972	4.2	6.4	28.3
2005	3,677,000	167,018	81,160	239,149	4.3	6.5	28.2
2006(Budget)	3,756,000	157,974	88,632	246,606	4.2	6.6	28.5

Notes : The figures for Personal Income in FY 1950 and 1955 are based on the former SNA and are not consistent with successive figures. The figure of national income in 2005 is estimated one.

3. Income Tax threshold

(In thousand yen)

Applicable Year	Single	Married couple without child	Married couple with one child	Married couple with two chil- dren
1950	29	43	57	71
1955	93	143	174	205
1960	118	210	250	289
1965	196	351	413	474
1970	344	580	728	880
1971	392	651	824	1,003
1972	405	672	852	1,037
1973	439	710	916	1,121
1974	705	950	1,181	1,507
1975	800	1,073	1,418	1,830
1976	800	1,073	1,418	1,830
1977	831	1,136	1,569	2,015
1978	831	1,136	1,569	2,015
1979	831	1,136	1,569	2,015
1980	831	1,136	1,569	2,015
1981	831	1,136	1,569	2,015
1982	831	1,136	1,569	2,015
1983	831	1,136	1,569	2,015
1984	967	1,322	1,833	2,357
1985	967	1,322	1,833	2,357
1986	967	1,322	1,833	2,357
1987	967	1,551	2,091	2,615
1988	967	1,556	2,095	2,619
1989	1,075	1,928	2,484	3,198
1990	1,075	1,928	2,484	3,198
1991	1,075	1,928	2,484	3,198
1992	1,075	1,928	2,484	3,198
1993	1,075	1,928	2,484	3,277
1994	1,075	1,928	2,484	3,277
1995	1,107	2,095	2,698	3,539
1996	1,107	2,095	2,698	3,539
1997	1,107	2,095	2,698	3,539
1998	1,107	2,095	2,698	3,616
1999	1,107	2,095	2,857	3,821
2000	1,144	2,200	2,833	3,842
2001	1,144	2,200	2,833	3,842
2002	1,144	2,200	2,833	3,842
2003	1,144	2,200	2,833	3,842
2004	1,144	1,566	2,200	3,250
2005	1,144	1,566	2,200	3,250
2006	1,114	1,566	2,200	3,250

- Notes: 1. Minimum taxable income is calculated by adding up the basic exemption, exemptions for spouses and dependents, employment income deductions, and social insurance premium deductions.
2. Figures are for the initial year of the revised tax law.
3. In and after 1989, in the case of married couples with two children, one of the children is subject to special dependents taxation.
4. In 1999, in the case of a married couple with one child, the child is under 16 years of age. In the case of a married couple with two children, one of the children is subject to special dependents taxation and the other one is under 16 years of age.

4. Number of Taxpayers and Income for Various Classes of Income (2004)

(a) Wage Earners

Class of Income (Per million yen)		2004			
		Number of Tax- payers (10 thousand)	Ratio %	Tax amount (In 100 million yen)	Ratio %
Not over	1	52	1.4	133	0.2
Not over	2	444	11.7	1,376	1.6
Not over	3	643	16.9	4,400	5.0
Not over	5	1,319	34.6	15,579	17.7
Not over	10	1,133	29.8	30,452	34.6
Over	10	218	5.7	36,048	41.0
Total		3,808	100.0	87,988	100.0

- Notes: 1. The figures are based on the results of wage research conducted by the National Tax Agency.
2. Income denotes gross revenue before various deductions.

(b) Taxpayers Filing Returns

Class of Income (Per million yen)		2004			
		Number of Tax- payers (10 thousand)	Ratio %	Tax amount (In 100 million yen)	Ratio %
Not over	1	40	5.3	56	0.2
Not over	2	188	25.3	539	2.2
Not over	3	158	21.2	933	3.9
Not over	5	150	20.2	1,762	7.3
Not over	10	128	17.2	3,320	13.8
Over	10	81	10.8	17,447	72.5
Total		744	100.0	24,058	100.0

Source: Based on the statistics from the National Tax Agency.

- Notes: 1. Income denotes gross income before various deductions.
2. In case where a wage earner in table (a) files a return, the person is counted in table (b) as well, thereby resulting in double counting.

Appendix V CORPORATION TAX BURDEN

1. Shares of Corporation Tax and Income Tax in Total National Tax Revenue

(In 100 million yen)

Fiscal Year	Item	Total National Tax Revenue	Corporation Tax		Income Tax	
			Amount	%	Amount	%
1950		5,702	838	14.7	2,201	38.6
1955		9,364	1,921	20.5	2,787	29.8
1960		18,010	5,734	31.8	3,906	21.7
1965		32,785	9,271	28.3	9,704	29.6
1970		77,733	25,672	33.0	24,282	31.2
1975		145,042	41,279	28.5	54,823	37.8
1976		168,020	47,920	28.5	62,125	37.0
1977		184,341	55,662	30.2	65,784	35.7
1978		232,239	79,128	34.1	77,530	33.4
1979		249,566	73,859	29.6	92,720	37.2
1980		283,688	89,227	31.5	107,996	38.1
1981		304,551	88,225	29.0	119,804	39.3
1982		320,031	91,346	28.5	128,455	40.1
1983		341,621	98,245	28.8	136,429	39.9
1984		367,748	113,402	30.8	140,638	38.2
1985		391,502	120,207	30.7	154,350	39.4
1986		428,510	130,911	30.6	168,267	39.3
1987		478,068	158,108	33.1	174,371	36.5
1988		521,938	184,381	35.3	179,538	34.4
1989		571,361	189,933	33.2	213,815	37.4
1990		627,798	183,836	29.3	259,955	41.4
1991		632,110	165,951	26.3	267,493	42.3
1992		573,964	137,136	23.9	232,314	40.5
1993		571,142	121,379	21.3	236,865	41.5
1994		540,007	123,631	22.9	204,175	37.8
1995		549,630	137,354	25.0	195,151	35.5
1996		552,261	144,833	26.2	189,649	34.3
1997		556,007	134,754	24.2	191,827	34.5
1998		511,977	114,232	22.3	169,961	33.2
1999		492,139	107,951	21.9	154,468	31.4
2000		527,209	117,472	22.3	187,889	35.6
2001		499,684	102,578	20.5	178,065	35.6
2002		458,442	95,234	20.8	148,122	31.1
2003		453,694	101,152	22.3	139,146	30.7
2004		481,029	114,437	23.8	150,954	31.4
2005		522,905	132,736	25.4	167,018	31.9
2006 (Budget)		509,243	130,580	25.6	157,974	31.0

Notes: The figures for 1978 are for 13 months (5/1978 ~5/1979).

2. Stratification of Corporations by Capitalization (2004)

(Amount:100 million yen)

Capital		Corporations		Total Sales	Tax Amount
		Number	Per cent of Total		
Over	Not over				
	1 million yen	25,478	1.0	36,123	280
1 million yen	5 million yen	1,088,716	42.3	876,888	2,632
5 million yen	10 million yen	303,498	11.8	352,599	1,304
10 million yen	50 million yen	1,060,016	41.2	3,737,817	22,881
50 million yen	100 million yen	52,952	2.1	1,096,451	9,047
100 million yen	1 billion yen	30,804	1.2	2,378,334	16,487
1 billion yen	5 billion yen	4,570	0.2	1,278,973	11,223
5 billion yen	10 billion yen	1,004	0.0	697,306	5,422
10 billion yen		1,321	0.1	3,372,333	44,272
Consolidated Corporation		294	0.0	668,043	983
Subsidiary		3,435	0.1	—	—
Total		2,572,088	100.0	14,494,869	114,531

Source : Annual Statistics Report, National Tax Agency

Appendix VI INHERITANCE TAX BURDEN

(Amount : 100 million yen)

Item Fiscal Year	Total Number of Decedents (A)	Number of Decedents with Taxable Property (B)	(B) / (A) %	Taxable Value of the Estate	Inheritance Tax	Minimum Taxable Amount of Property
						(After 1958)
1961	695,644	11,342	1.6	981	160	¥1,500,000 + ¥300,000 × number of statutory heirs
1965	700,438	13,407	1.9	2,091	410	¥2,500,000 + ¥500,000 × number of statutory heirs
1970	712,962	24,454	3.4	7,011	1,342	¥4,000,000 + ¥800,000 × number of statutory heirs + maximum amount of spousal exemption ¥2,000,000
1971	684,521	25,951	3.8	9,403	2,074	¥4,000,000 + ¥800,000 × number of statutory heirs + maximum amount of spousal exemption ¥4,000,000
1972	683,751	30,211	4.4	12,201	2,604	
1973	706,416	29,231	4.1	16,231	3,754	¥6,000,000 + ¥1,200,000 × number of statutory heirs + maximum amount of spouse exemption ¥6,000,000
1974	710,510	32,898	4.6	18,966	4,377	
1975	702,275	14,593	2.1	15,121	1,973	¥20,000,000 + ¥4,000,000 × number of statutory heirs
1980	772,801	26,797	3.7	30,215	4,399	
1981	720,262	31,549	4.4	38,281	5,427	
1982	711,883	35,922	5.0	44,729	6,330	
1983	470,038	39,534	5.3	50,021	7,153	
1984	740,255	43,012	5.8	54,287	7,769	
1985	752,259	48,111	6.4	62,463	9,261	
1986	750,620	51,847	6.9	67,637	10,443	
1987	751,172	59,008	7.9	82,509	14,343	
1988	793,014	36,468	4.6	96,380	15,629	
1989	788,594	41,655	5.3	117,686	23,930	¥40,000,000 + ¥8,000,000 × number of statutory heirs
1990	820,305	48,287	5.9	141,058	29,527	
1991	829,797	56,554	6.8	178,417	39,651	¥48,000,000 + ¥9,500,000 × number of statutory heirs
1992	856,643	54,449	6.4	188,201	34,099	
1993	878,532	52,877	6.0	167,545	27,768	¥50,000,000 + ¥10,000,000 × number of statutory heirs
1994	875,933	45,335	5.2	145,454	21,058	
1995	922,139	50,739	5.5	153,000	21,730	
1996	896,211	48,476	5.4	140,774	19,376	
1997	913,402	48,611	5.3	138,635	19,339	
1998	936,484	49,526	5.3	132,468	16,826	
1999	982,031	50,731	5.2	132,699	16,876	
2000	961,653	48,463	5.0	123,409	15,213	
2001	970,331	46,012	4.7	117,035	14,771	
2002	982,379	44,370	4.5	106,397	12,863	
2003	1,014,951	44,438	4.4	103,582	11,263	
2004	1,028,602	43,488	4.2	98,618	10,651	

Source : The Annual Statistics Report of the National Tax Agency

Appendix VII

1. Revenue from National Taxes; FY1998 – 2006

Tax Item	1998		1999		2000		2001	
	Amount	%	Amount	%	Amount	%	Amount	%
Direct Taxes (Total)	303,397	59.3	281,293	57.2	323,193	61.3	297,393	59.5
Income Tax	169,961	33.2	154,468	31.4	187,889	35.6	178,065	35.6
Corporation Tax	114,232	22.3	107,951	21.9	117,472	22.3	102,578	20.5
Special Corporation Surtax	7	0.0	2	0.0	1	0.0	–	–
Special Provisional Corpora- tion Surtax (s)	2	0.0	–	–	–	–	–	–
Inheritance Tax	19,156	3.7	18,853	3.8	17,822	3.4	16,745	3.4
Land Value Tax	39	0.0	17	0.0	9	0.0	8	0.0
Income Tax *(s)	–	–	–	–	–	–	–	–
Indirect Taxes, etc. (Total)	208,580	40.7	210,846	42.8	204,016	38.7	202,291	40.5
Consumption Tax	100,744	19.7	104,471	21.2	98,221	18.6	97,671	19.5
Liquor Tax	18,983	3.7	18,717	3.8	18,164	3.4	17,654	3.5
Tobacco Excise Tax	10,462	2.0	9,050	1.8	8,755	1.7	8,614	1.7
Gasoline Tax	19,982	3.9	20,707	4.2	20,752	3.9	20,981	4.2
Liquid Petroleum Gas Tax	144	0.0	144	0.0	142	0.0	140	0.0
Aviation Fuel Tax	901	0.2	872	0.2	880	0.2	883	0.2
Petroleum Tax	4,767	0.9	4,859	1.0	4,890	0.9	4,718	0.9
Commodity Tax	–	–	–	–	–	–	–	–
Bourse Tax	190	0.0	–	–	–	–	–	–
Securities Transaction Tax	1,726	0.3	△ 2	0.0	0	0.0	0	0.0
Motor Vehicle Tonnage Tax	8,165	1.6	8,431	1.7	8,507	1.6	8,536	1.7
Customs Duty	8,687	1.7	8,102	1.6	8,215	1.6	8,518	1.7
Tonnage Due	86	0.0	87	0.0	88	0.0	86	0.0
Stamp Revenue	16,084	3.1	15,615	3.2	15,318	2.9	14,288	2.9
Local Road Tax*(s)	2,850	0.6	2,934	0.6	2,962	0.6	3,010	0.6
Liquefied Petroleum Gas Tax *(s)	144	0.0	144	0.0	142	0.0	140	0.0
Aviation Fuel Tax*(s)	164	0.0	159	0.0	160	0.0	161	0.0
Motor Vehicle Tonnage Tax *(s)	2,722	0.5	2,810	0.6	2,836	0.5	2,845	0.6
Special Tonnage Due(s)	107	0.0	109	0.0	111	0.0	107	0.0
Customs Duty on Oil(s)	518	0.1	536	0.1	550	0.1	497	0.1
Promotion of Power- Resources Development Tax (s)	3,573	0.7	3,651	0.7	3,746	0.7	3,686	0.7
Gasoline Tax(s)	6,654	1.3	6,716	1.4	6,934	1.3	7,155	1.4
Special Tobacco Tax(s)	927	0.2	2,736	0.6	2,644	0.5	2,602	0.5
Total	511,977	100.0	492,139	100.0	527,209	100.0	499,684	100.0

Note 1: Taxes marked with (s) are those with revenues distributed to Special Accounts.

2: Taxes marked with asterisks are those with revenues distributed to local governments.

REVENUE

(In 100 million yen)

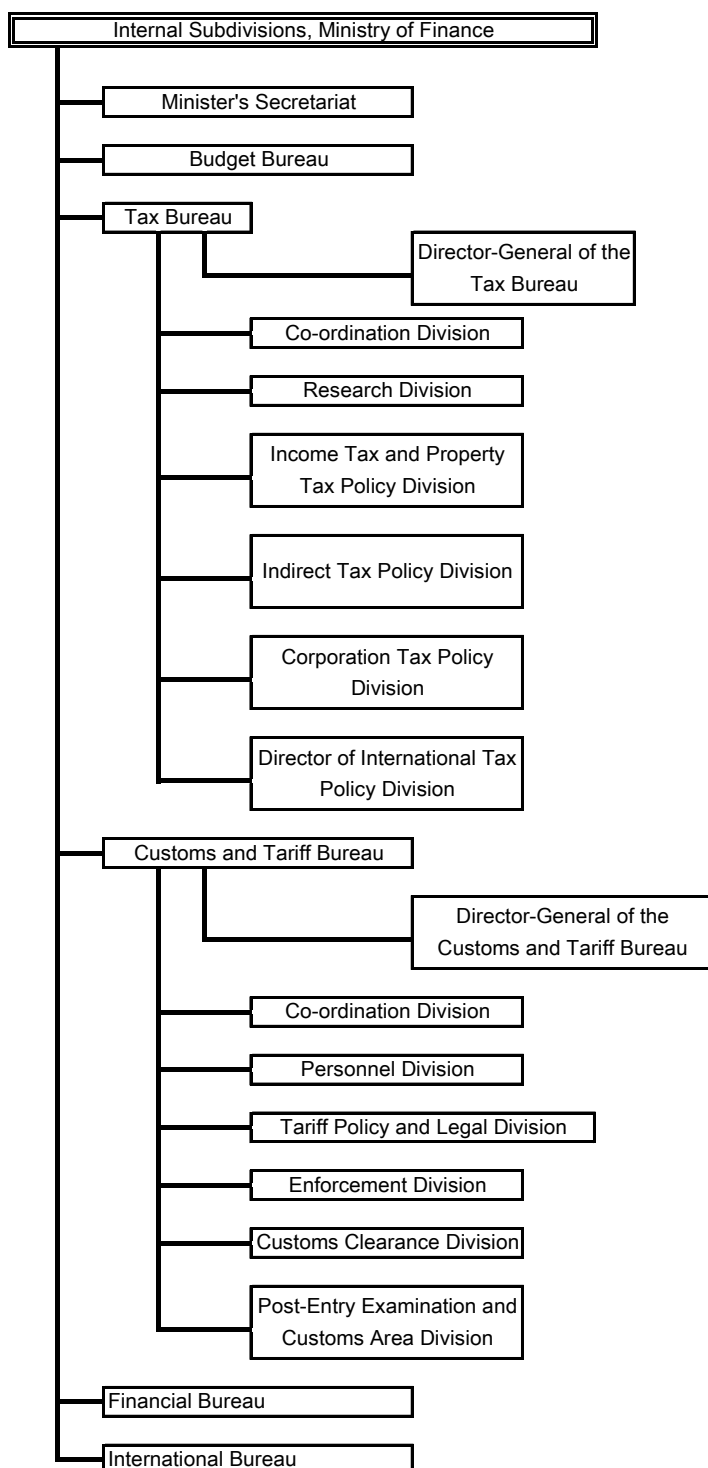
2002		2003		2004		2005		2006 (Budget)	
Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
257,891	56.3	254,727	56.1	279,858	58.2	315,412	60.3	302,354	59.4
148,122	32.3	139,146	30.7	146,705	30.5	155,859	29.8	127,880	25.1
95,234	20.8	101,152	22.3	114,437	23.8	132,736	25.4	130,580	25.6
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
14,529	3.2	14,425	3.2	14,465	3.0	15,657	3.0	13,800	2.7
5	0.0	3	0.0	2	0.0	2	0.0	-	-
-	-	-	-	4,249	0.9	11,159	2.1	30,094	5.9
200,551	43.7	198,967	43.9	201,171	41.8	207,492	39.7	206,889	40.6
98,115	21.4	97,128	21.4	99,743	20.7	105,834	20.2	105,380	20.7
16,804	3.7	16,842	3.7	16,599	3.5	15,853	3.0	15,720	3.1
8,441	1.8	9,032	2.0	9,097	1.9	8,867	1.7	9,400	1.8
21,263	4.6	21,821	4.8	21,910	4.6	21,676	4.1	21,560	4.2
142	0.0	143	0.0	143	0.0	142	0.0	140	0.0
901	0.2	910	0.2	880	0.2	886	0.2	870	0.2
4,634	1.0	4,783	1.1	4,803	1.0	4,931	0.9	4,760	0.9
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
8,480	1.8	7,671	1.7	7,488	1.6	7,574	1.4	7,370	1.4
7,936	1.7	8,029	1.8	8,177	1.7	8,857	1.7	9,060	1.8
87	0.0	88	0.0	90	0.0	91	0.0	90	0.0
13,638	3.0	11,651	2.6	11,350	2.4	11,688	2.2	12,170	2.4
3,035	0.7	3,087	0.7	3,101	0.6	3,112	0.6	3,098	0.6
142	0.0	143	0.0	143	0.0	142	0.0	140	0.0
164	0.0	165	0.0	160	0.0	161	0.0	158	0.0
2,827	0.6	3,835	0.8	3,744	0.8	3,787	0.7	3,685	0.7
109	0.0	110	0.0	113	0.0	114	0.0	113	0.0
415	0.1	421	0.1	442	0.1	446	0.1	5	0.0
3,768	0.8	3,663	0.8	3,726	0.8	3,592	0.7	3,540	0.7
7,102	1.5	7,033	1.6	7,072	1.5	7,408	1.4	7,393	1.5
25,50	0.6	2,411	0.5	2,389	0.5	2,329	0.4	2,237	0.4
458,442	100.0	453,694	100.0	481,029	100.0	522,905	100.0	509,243	100.0

2. Revenue from Local Taxes ; FY2003-2006

(In 100 million yen)

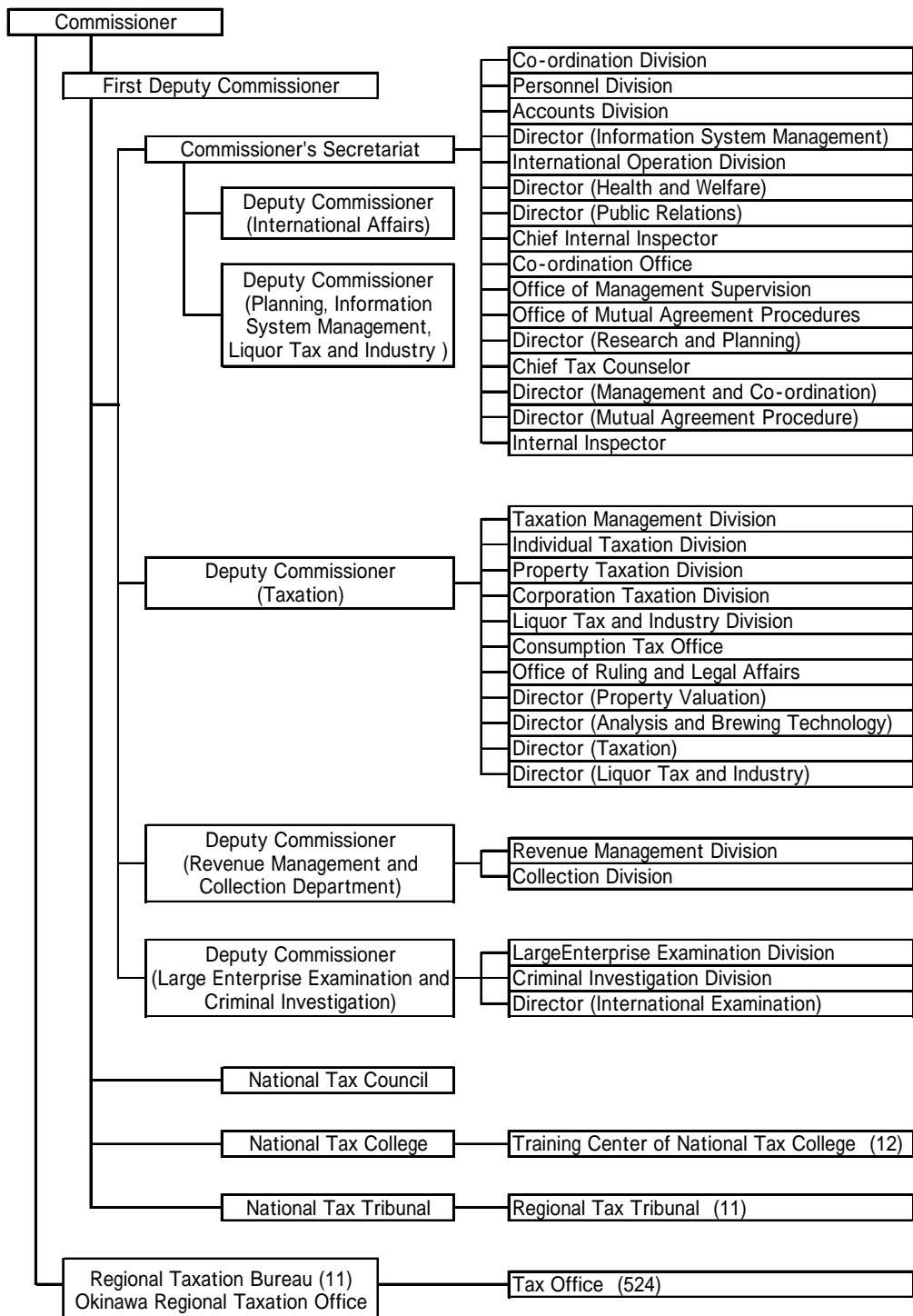
Item	2003		2004		2005 (Estimated)		2006 (Estimated)	
	Amount	%	Amount	%	Amount	%	Amount	%
1. Prefectural Tax (Total)	136,931	100.0	144,870	100.0	142,737	100.0	154,308	100.0
(1) Ordinary Tax	121,393	88.7	129,294	89.2	127,500	89.3	138,921	90.0
Prefectural Inhabitants Tax	32,734	23.9	33,986	23.5	33,357	23.4	35,973	23.3
Enterprise Tax	38,458	28.1	43,389	30.0	43,462	30.4	50,593	32.8
Local Consumption Tax	23,936	17.5	26,139	18.0	25,061	17.6	26,343	17.1
Real Property Acquisition Tax	4,805	3.5	4,564	3.2	4,473	3.1	4,828	3.1
Prefectural Tobacco Excise Tax	2,778	2.0	2,826	2.0	2,682	1.9	2,848	1.8
Golf Course Utilization Tax	691	0.5	638	0.4	606	0.4	583	0.4
Special Local Consumption Tax	2	0.0	1	0.0	—	—	—	—
Automobile Tax	17,463	12.8	17,131	11.8	17,713	12.4	17,659	11.4
Mine-lot Tax	4	0.0	4	0.0	4	0.0	4	0.0
Hunters' License Tax	16	0.0	—	—	—	—	—	—
Prefectural Property Tax	155	0.1	165	0.1	142	0.1	90	0.1
Other ordinary taxes not stipulated in the Local Tax Law	351	0.3	451	0.3	—	—	—	—
(2) Earmarked Taxes	15,539	11.3	15,576	10.8	15,237	10.7	15,387	10.0
(3) Transitional Revenue from repealed taxes	0	0.0	0	0.0	—	—	—	—
2. Municipal Tax (Total)	189,726	100.0	190,518	100.0	190,452	100.0	194,675	100.0
(1) Ordinary Tax	173,207	91.3	174,001	91.3	173,881	91.3	178,608	91.7
Municipal Inhabitants Tax	76,366	40.3	76,686	40.3	76,818	40.3	84,333	43.3
Property Tax	86,786	45.7	87,078	45.7	87,243	45.8	83,912	43.1
Light Vehicle Tax	1,405	0.7	1,459	0.8	1,519	0.8	1,573	0.8
Municipal Tobacco Excise Tax	8,538	4.5	8,680	4.6	8,240	4.3	8,750	4.5
Mineral Product Tax	14	0.0	14	0.0	14	0.0	15	0.0
Special Landholding Tax	91	0.0	75	0.0	47	0.0	25	0.0
Other ordinary taxes not stipulated in the Local Tax Law	6	0.0	10	0.0	—	—	—	—
(2) Earmarked taxes	15,637	8.2	15,534	8.2	15,462	8.1	14,988	7.7
(3) Transitional revenue from repealed taxes, and others	882	0.5	983	0.5	1,109	0.6	1,079	0.6

Appendix VIII ORGANISATIONAL CHART FOR THE MINISTRY OF FINANCE



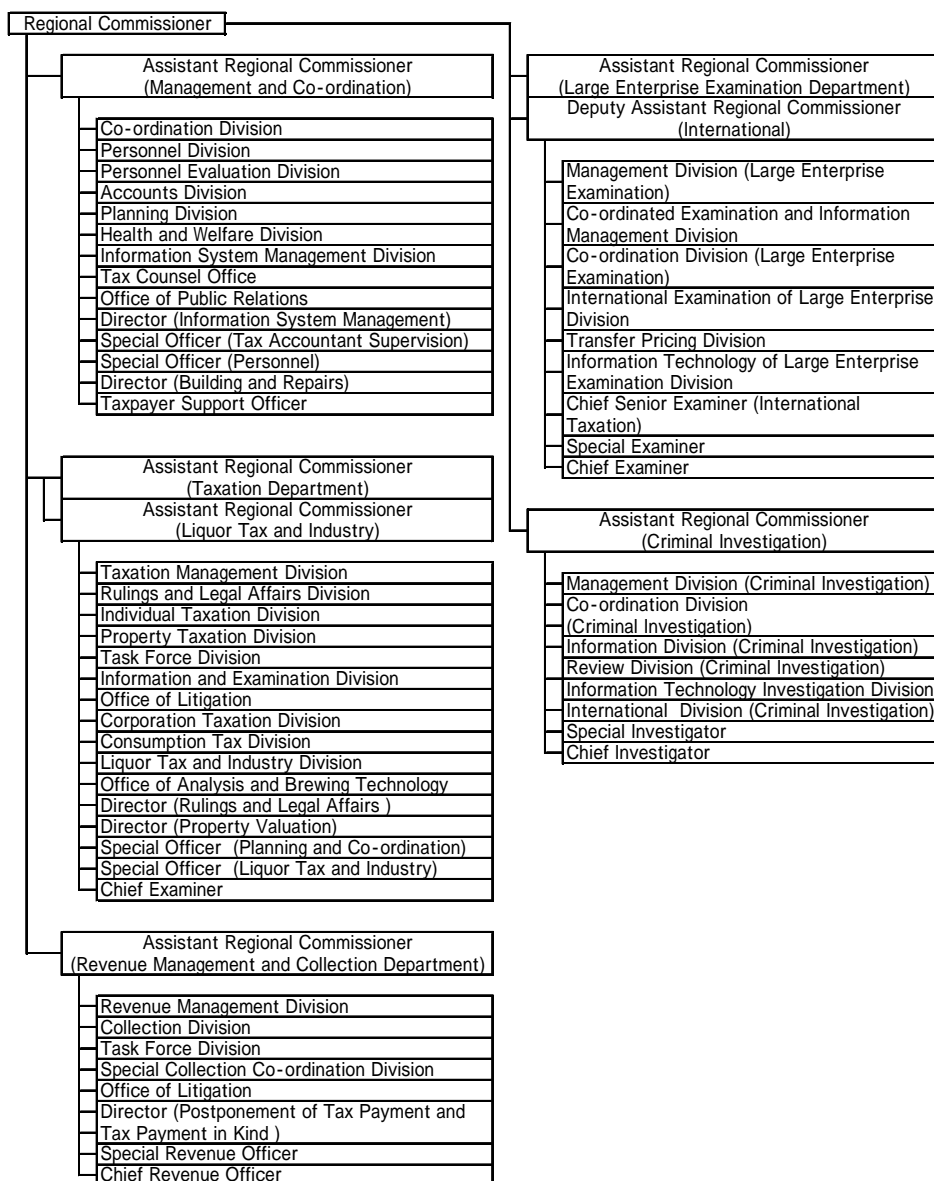
Appendix IX ORGANISATIONAL CHART FOR

Organization Chart of the NTA



NATIONAL TAX AGENCY (in FY 2005)

Organization Chart of Regional Taxation Bureau (except Okinawa)



Organization Chart of Tax Office

