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DOING BUSINESS

IN JAPAN

The network for doing business

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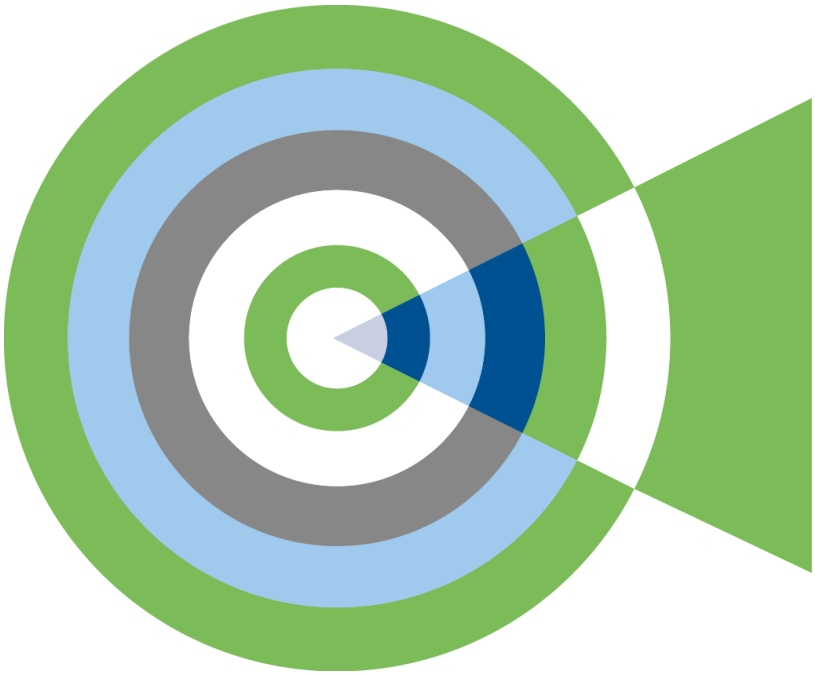

1 – INTRODUCTION

UHY is an international organisation providing accountancy, business management and consultancy services through financial business centres in over 80 countries throughout the world.

Business partners work together through the network to conduct transnational operations for clients as well as offering specialist knowledge and experience within their own national borders. Global specialists in various industry and market sectors are also available for consultation.

This detailed report providing key issues and information for investors considering business operations in Japan has been provided by the office of UHY representatives:

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A detailed firm profile for UHY's representation in Japan can be found in section 8.

Information in the following pages has been updated so that they are effective at the date shown, but inevitably they are both general and subject to change and should be used for guidance only. For specific matters, investors are strongly advised to obtain further information and take professional advice before making any decisions. This publication is current at September 2013.

We look forward to helping you do business in Japan.

2 – BUSINESS ENVIRONMENT

Japan is one of the world's economic superpowers and its prosperity is based on its efficient industries (automobile, information and communication technology and consumer electronics).

Japan has accelerated high-level technology development in the environmental, medical care and biotechnology sectors. Japan has also promoted a culture-oriented industry referred to as 'Cool Japan'.

COUNTRY BACKGROUND

POPULATION

Japan has an approximate population of 127 million inhabitants, with an average population density of 336 people per square kilometre (490 per square mile).

AREA

Japan covers 377,930km² and is made up of 47 local government districts.

LANGUAGE

The national language is Japanese.

Since most Japanese people study English during their time as a student, English is the most popular foreign language.

LEGAL SYSTEM

The Japanese constitution provides the democratic foundation for the separation of state powers (ie legislative, judicial and governmental). Judicial power is vested in the Supreme Court and lower courts established by law. Lower courts are divided into four bodies: high courts, district courts, family courts and summary courts.

CURRENCY

Japan's currency is the yen (JPY).

COST OF LIVING

The standard of living and living costs in Japan are known for being one of the highest in the world. Some of the world's most expensive real estate is found in central Tokyo. However, real estate prices in Tokyo have been declining since the massive earthquake in March 2011.

EMPLOYMENT

The Japanese labour market was characterised by lifetime employment until the mid-90s, but since then there has been a prevailing trend of irregular employment. In 2012, the labour force was 62.9 million, with unemployment standing at 4.5%.

ECONOMY

GROSS DOMESTIC PRODUCT (GDP)

In 2011, the nominal GDP was 555 trillion yen (USD 5.8 trillion), the third largest in the world after the United States and China.

RECENT ECONOMIC HISTORY

Japan suffered a long-term economic recession during the 1990s after its assets price bubble in the late 1980s broke. The government adopted policies to promote exports and Japan's economy experienced a gradual recovery trend from 2003–2007, with steady economic growth.

However, the global financial crisis dried up global demand for Japan's exports and Japan went into recession in 2008. Government stimulus spending helped to bring the Japanese economy back on track in late 2009 and 2010.

Subsequently, the massive earthquake in March 2011 caused enormous damage in the north-eastern coastal region and Japan is facing rebuilding struggles.

MAIN TRADING PARTNERS (2012)

TABLE 1

Main export destinations

COUNTRIES	% OF TOTAL EXPORTS
People's Republic of China	21.2
United States	17.5
South Korea	7.7
Taiwan	5.7
Thailand	5.4
Hong Kong	5.1
Singapore	2.9
Germany	2.6
Indonesia	2.5
Australia	2.3

TABLE 2

Main countries of origin for imports

COUNTRIES	% OF TOTAL IMPORTS
People's Republic of China	21.2
United States	8.6
Australia	6.3
Saudi Arabia	6.1
UAE	4.9
South Korea	4.5
Malaysia	3.6
Indonesia	3.6
Germany	2.7
Thailand	2.6

STOCK EXCHANGE

The Tokyo Stock Exchange (TSE) is the third largest stock exchange in the world. TSE had 2,308 listed companies with a combined market capitalisation of USD 3.4 trillion as of February 2013.

TSE is broken into three separate parts: large companies, mid-sized companies and the market of the high-growth and emerging stocks ('mothers') for venture companies. The Osaka Securities Exchange (OSE) and Nagoya Stock Exchange (NSE) are also important stock exchanges in Japan.

3 – FOREIGN INVESTMENT

There are a number of reasons for investing in Japan.

Key reasons why foreign investors are attracted to Japan are because the country offers:
- A large consumer market with a population over 127 million
- A financial centre
- A key trading hub in Asia
- A high degree of control over the Asian market
- Highly advanced technology
- A leading centre for innovation, research and development in Asia.

INVESTMENT SUPPORT

JAPAN EXTERNAL TRADE ORGANISATION (JETRO)

JETRO is a governmental organisation with more than 70 overseas offices in over 50 countries across the world. For foreign companies planning to start a business in Japan, JETRO's Invest Japan Business Support Centre (IBSC) will provide consultation advice and facilities for establishing a business base.

JETRO IBSC staff and advisors provide information and consultation advice, including on:
- Market and industry information
- Relevant legal systems
- Taxation, labour and legal issues
- Networking with potential business partners
- Finding human resources and an office location
- Information on the regulations and incentives from national and local governments.

National and local authorities offer a number of incentives to promote investment. These include:
- Preferential tax policies such as reduction or exemption of business taxes
- Preferential fixed asset taxes and real estate acquisition taxes
- Subsidies
- The provision of land and buildings
- Preferential taxes related to financing and lending systems.

In addition to information on these incentives, IBSC can arrange meetings with representatives from national and local authorities.

THE OFFICE OF TRADE AND INVESTMENT OMBUDSMAN (OTO)

The Office of Trade and Investment Ombudsman (OTO) is a government body for the promotion of investment from abroad. OTO is the contact point when problems arise due to government regulations for export to or investment in Japan. OTO can contact relevant government ministries and agencies including customs houses, counsellor offices, regional economic trade and industry bureaus, general quarantine offices, animal quarantine stations, plant epidemic prevention stations, regional transport bureaus, embassies and consulates, as well as JETRO offices.

4 – SETTING UP A BUSINESS

Foreign investors who intend to set up a business in Japan can choose from a wide range of legal entities.

The most common legal entities in Japan are:
- Representative offices
- Branch offices
- Companies (private).

It is possible to choose another entity type depending on the situation.

REPRESENTATIVE OFFICE

Before officially starting business in Japan, foreign investors can use representative offices as a temporary basis for preparation of their activities.

Direct business operations are not permitted for representative offices, only indirect business operations such as market surveys, collecting information and advertising. A representative office is not allowed to open bank accounts or lease real estate in its own name. For such activities, a headquarters' manager or a representative office manager must use his/her name. The establishment of a representative office does not need to be registered with any administrative authorities.

Set-up procedures for a representative office are outlined in Table 3 below.

TABLE 3
Setting up a representative office

POINT	REPRESENTATIVE OFFICE
Purpose	To gather information and advertise in Japan
Tax Condition	Not considered as a 'permanent establishment' (PE) in Japan
Set-up procedures	1) Establish a representative office 2) Acquire a certificate of status of residence from the Ministry of Justice's Immigration Bureau 3) Submit certificate of status of residence to the Japanese consulate in the representative's home country and a Japanese consulate visa 4) After entering Japan, the representative determines a place of residence and performs alien registration procedures 5) Open bank account (in the case of a representative office only a personal account can be opened) 6) Register employee information with the Labour Standards Inspection office, Public Employment Security office, Social Insurance office and Tax office (for wage payment related information)
Conditions for a non-PE	1) Branch, plant or other operating resident entity in Japan 2) Working for over one year to construct a building in Japan 3) An attorney is needed for the foreign company 4) No tax for a non-PE

	5) If a representative office receives income on the sale or rental of real estate or receives interest and dividends (withholding tax 20%), tax is imposed.

BRANCH OFFICE

Foreign investors may find setting up a branch office is the simplest way to establish a business base in Japan.

A branch office can start business operations after deciding a base of operation, appointing the branch representative and registering all the necessary information. A Japanese branch office can open bank accounts and lease real estate in its own name. However, a branch office does not have independent corporate status. It is treated as a part of a foreign company incorporated overseas. The foreign company is ultimately responsible for all the debts and credits incurred by the business activities of its Japanese branch.

CORPORATION

When foreign companies intend to establish a subsidiary of their existing business in Japan, they must choose a corporation type.

Japanese Corporation Law recognises four types of company entity:

- Joint-stock corporation (*Kabushiki-Kaisha* – K.K.)
- Limited liability company (*Godo-Kaisha* – GK)
- Unlimited partnership (*Gomei-Kaisha*)
- Limited partnership (*Goshi-Kaisha*).

The last two types of company are granted corporate status under the Japanese Corporation Law, though rarely chosen in practice because equity participants bear unlimited liability.

All types of subsidiary companies are established by completing legal procedures and are required to be registered. Once the registration is processed, companies can open bank accounts, rent or lease property and engage in activities as a legal entity. A Japanese subsidiary company is considered a separate entity from the foreign company, so all debts and credits generated by a subsidiary belong to the subsidiary.

JOINT-STOCK CORPORATION (KABUSHIKI KAISHA – K.K)

A *Kabushiki-Kaisha* (K.K.) is the most common form of corporate entity used in Japan by foreign investors. Its shareholders' liability is limited to their capital contributions. The formation procedures for a K.K. are set out in Table 4 below.

TABLE 4

Setting up a joint-stock corporation

STEPS	INFORMATION/ACTIONS REQUIRED
1) Basic matters	Company name, company objectives, address of head office, paid-in capital, accounting period, bank for accepting share subscription money etc.

2) Search for similar company name	At the Legal Affairs Bureau
3) Preparation of articles of incorporation	Care should be taken over company objectives
4) Company seal	1) Acquire seal for the company and representatives at a seal carver 2) Obtain certificate seal registration at the Ward office
5) Promoter meeting	Preparation of minutes of the promoter meeting. Two copies of the meeting must be prepared
6) Notarisation of the articles of incorporation	Notarisation is done at a public notary office (stamp duty JPY 40,000 and a notary fee JPY 50,000)
7) Appointment of a bank to handle the share subscription money	The selection of a bank for future operations is very important
8) Public offering	Allotment of shares to the parent company
9) Payment of the share subscription money to the bank	
10) Certificate for the receipt of the share subscription money	Issued by the bank
11) Establishment meeting by the subscribers	Appoint directors and auditors
12) Board of director meeting	Approval of directors; minutes must be taken
13) Register of Establishment	Application for registration (with a registered representative seal); registration and licence tax of JPY 150,000 or 0.7% of paid in capital
14) Surrender the shares	
15) Notification under the Foreign Exchange Law	Register with the Bank of Japan within 15 days
16) Tax registration	With Legal Affairs (Tax, Social Securities and Labour office)

LIMITED LIABILITY COMPANY (*GODO KAISHA* – GK)

A *Godo-Kaisha* (GK) is an entity loosely based on the US LLC. The investor's liability in the GK is limited to their capital contribution. A GK is more flexible than a K.K. and well-suited for smaller companies.

Unlike the US LLC, a GK is not available for pass-through income taxation for Japanese tax purposes. The formation and legal structure of a GK is similar to that of a K.K. but much simpler. Unlike a K.K., each GK member is responsible for managing the affairs of and representing the GK.

UNLIMITED PARTNERSHIP (*GOMEI-KAISHA*)

A *Gomei-Kaisha* is a company with unlimited liability members. They are jointly and severally responsible for the company's liabilities.

LIMITED PARTNERSHIP (*GOSHI-KAISHA*)

A *Goshi-Kaisha* is similar to a *Gomei-Kaisha* except there are members with unlimited liability and with limited liability.

OVERVIEW FOR NEW INVESTORS

A foreign company may invest in Japan using a method other than those described above, for example, by establishing a joint venture with a Japanese company or equity participation in a Japanese company.

The following section provides a summary regarding the main methods of setting up a business ie representative offices, branches and corporations, as a comparison guide for new foreign investors. Table 5 shows the general factors which should be checked before determining the entry type.

TABLE 5

Factors to consider when choosing a representative office, branch or subsidiary

TYPE	FACTORS TO BE CHECKED
Representative Office	a) Not permissible to conduct business operations b) For gathering information and communications only c) Purchase and hold materials only d) Difficult to get business trust from customers
Branch	a) Expand business slowly by trade or trade in Japan b) Possible to set off a starting-up loss with the HO income c) Impossible to deduct loan interest from the parent d) Convenient for a famous fashion brand company e) Useful for conversion into a domestic company
Corporation	a) To expand business faster by business operation in Japan b) Not necessary to disclose the parent company's accounts c) To avoid HO director appearing in a Japanese court d) Possible to deduct loan interest from the parent e) Necessary to consider tax treaty and foreign tax deductions f) Possible to get social insurance or benefits g) Easy to employ new staff h) Easy to gain trust from customers i) Easy to get a loan from the bank and government.

COMPARISON OF CORPORATIONS VERSUS BRANCHES

Most foreign investors choose a corporation or branch as their business entity in Japan. It is possible to establish a branch or transfer to a corporation after a couple of years.

TABLE 6
Comparison between a corporation and a branch

POINT	CORPORATION	BRANCH
Capital	No limit	N/A
Dividends or profit	Remittance subject to withholding tax at 20% (or reduced rates under tax treaty)	N/A
Loan:		
• Loan from HO	N/A	Interest is not deductible
• Loan from parent	Interest is deductible (thin capitalisation rules)	Interest is deductible (thin capitalisation rules)
• Loan from bank	Possible	Difficult
Annual administration	Annual shareholders' meeting	No annual procedure Update registered items
Tax return	Submitted by the subsidiary	Submitted by the branch with the parent's accounts
Director	At least one representative director who is a resident of Japan	Not necessary
Hiring new staff	Attractive for employees	Not attractive for employees

5 – LABOUR

There have been major changes to the employment environment in Japan in the last 20 years.

In 1999 and 2003, the government revised the Worker Dispatch Law, which fundamentally eased regulations on the use of temporary workers. This made the use of temporary work prevalent in Japanese companies.

TYPES OF EMPLOYMENT

Employment in Japan is classified into two categories:

- Regular
- Temporary (part-time and dispatch).

REGULAR EMPLOYMENT

Regular employment (often referred as 'permanent employment' in Japan) is regular full-time employment that includes benefits, such as health insurance, paid time off and retirement allowance.

Most Japanese companies traditionally used permanent employment and many people regarded their employment as a life-time assignment. However, the permanent employment system inevitably raised personnel costs with regards to maintaining senior employees. To cope with an increasingly open economy and build international competitive advantage, the government adopted policies of labour market deregulation such as the revision of the Worker Dispatch Law.

TEMPORARY EMPLOYMENT

Temporary employment refers to a situation where the employee is expected to leave the employer within a certain period of time. Temporary workers may work full-time or part-time, depending on the individual case.

PART-TIME

Part-time workers have shorter working hours per week than regular workers in the same place of work. In some cases part-time workers are given benefits (such as health insurance) but not a full benefit package. Regular pay hikes, bonus payments and retirement allowances are generally not applied to this type of worker.

However, the Part-Time Employment Act was revised to protect part-time workers. For example, it stipulates that part-time workers' abilities should be used effectively and working conditions should be equal to those of regular employees in the same workplace.

DISPATCH

Dispatch workers are workers who have employment contracts with temporary work agencies. The agencies send dispatch workers to companies in need of short-term staff. Dispatch workers are also used in work that has a cyclical nature which requires frequent adjustment of staffing levels. The Worker Dispatch Law prohibits the use of dispatch workers in some industries, including port transport, construction, guard services and medical services.

WORKING CONDITIONS

Foreign employees are protected by the Labour Standards Law and other related laws which protect Japanese employees.

These laws are designed to ensure that there is no discrimination or unfair treatment of employees.

WORK PERMITS AND VISAS

Employers are only able to employ individuals who have permission to live and work in Japan. Generally, foreigners who have one of the following residential statuses have the right to work in Japan:

- Permanent resident
- Spouse or child of Japanese national
- Spouse or child of permanent resident
- Long-term resident.

Foreigners are permitted to work as the following or in the following professions/services:

- Professor
- Artist
- Religious activities
- Journalist
- Investor/business manager
- Legal/accounting services
- Medical services
- Researcher
- Instructor
- Engineer
- Specialist in humanities and international services
- Intra-company transferee
- Entertainment
- Skilled labour
- Designated activities.

More detailed information is provided by the Immigration Bureau of Japan.

CONTRACT OF EMPLOYMENT

Employers are required to enter into labour contracts with employees. Employers also need to provide written notification about employment conditions, including:

- Place of work
- The duties that the employee will have to perform
- Working hours
- Holidays
- The methods of determining, calculating and paying wages
- Matters pertaining to resignation and dismissal.

PROBATION PERIOD

A permanent contract of employment will usually have a probation period of three months. Employers are allowed to terminate their relationship with an employee during or after the probation period if reasons of termination are objectively reasonable.

WAGES

Employers must pay wages to employees in full at least once a month, on a fixed date. Employers are also required to deduct income tax, social insurance premiums and similar expenses from wages of their employees.

GUARANTEE OF MINIMUM WAGES

The minimum wage depends on the industry and region. Industrial minimum wages are applied to certain industries and usually set higher than the regional minimum wages. If regional and industrial minimum wages differ, the higher of two will be applied.

As of 2010, regional minimum wages range from JPY 642–821 per hour for all workers. Minimum wages do not include costs of commuting, overtime pay and temporary pay. They must be paid exclusively to employees.

RETIREMENT BENEFIT

Most Japanese companies have some form of retirement benefits or severance pay system. Retirement benefits are calculated based on the length of service and reason for leaving the company. Retirement benefits are treated more favourably for tax purposes than ordinary pay.

EXTRA PAY

Employers must pay employees for overtime work, work on holidays and 'midnight' work. Japanese laws and regulations establish rules for how to calculate extra pay, which is paid on top of the regular wage. To determine overtime pay, the employer must calculate this at a rate of 25% or more of the regular wage, for work on holidays at least 35% and for work during the night (between the hours of 10pm–5am) at least 25%.

ADVANCE NOTICE OF DISMISSAL

When dismissing an employee, the advanced notice period is usually at least 30 days. If an employer fails to give timely advance notice with no reasonable excuse, the employer must pay the employee the amount of the average wage for the number of days falling short of the 30 days advanced notice.

WORKING HOURS, BREAKS AND DAYS OFF

The statutory working hours are eight hours a day, 40 hours a week. However, as an exception, working up to 44 hours a week is permitted for certain businesses. These businesses include retail and beauty services, theatres, businesses related to health and hygiene, as well as restaurants and entertainment businesses with less than ten regular employees.

Statutory holiday is one day a week or four days or more in a four week period.

LABOUR AND SOCIAL INSURANCE SYSTEMS

Employers are legally obliged to take part in labour and social insurance schemes. There are four kinds (listed below) of insurance systems, where employers pay their portion of insurance premiums to the authorities together with the employee's portion (which is deducted from the employee's wages):

1) Workers' Accident Compensation Insurance – covers work-related injuries and diseases including accidents while commuting to or from work
2) Employment Insurance – provides temporary financial assistance for unemployed people while they look for work or upgrade their skills
3) Health Insurance and Nursing Care Insurance – covers medical and nursing care expenses for employees
4) Employees' Pension Insurance – provides benefits for employees to cover the income of households after retirement and likely risks, such as disability and death.

Workers' Accident Compensation Insurance and Employment Insurance are referred to collectively as 'Labour insurance'. Health, Nursing Care and Employees' Pension Insurances are referred to collectively as 'Social Insurance'.

6 – TAXATION

RESIDENCY OF COMPANIES

For the purpose of applying the Corporation Tax Law of Japan, a company which is headquartered or has its main office in Japan is considered a domestic company.

A company is considered a foreign company if it is headquartered or has its main office outside of Japan.

Taxpayers subject to the Corporation Tax Law of Japan are corporations (including those established by special laws) under the company law or other corporation laws or under the civil code. This section focuses only on companies established under the company law of Japan or equivalent laws of foreign countries.

CORPORATE TAX

TAXATION OF DOMESTIC COMPANIES AND FOREIGN COMPANIES

A domestic company is liable to pay corporation tax on its worldwide income. A foreign company is liable to pay corporation tax on its domestic source income.

DOMESTIC INCOME

Domestic income is income from business conducted in Japan or from using, holding or transferring assets located in Japan. Domestic income includes income from conducting a business providing personal services in Japan, for the lending of real estate or any right on real estate located in Japan, interest from Japanese government bonds, dividends from domestic companies and other income as prescribed by the corporation tax law.

The scope and kinds of domestic source income subject to corporation tax varies with the type of permanent establishment (PE) held by a foreign company. Three types of PE are prescribed by the corporation tax law:

- Branch, factory or other fixed place of business (Item 1 PE)
- Activities of construction, installation or assembly (Item 2 PE)
- Agent of the foreign corporation (Item 3 PE).

TAXABLE INCOME AND TAX YEAR

Taxable income is net revenue less deductions (cost, expenses and losses). It is to be calculated in accordance with generally accepted accounting principles and the provisions of the corporation tax law. The tax year for the calculation of taxable income is to be the same as the accounting year used for financial reporting purposes.

A company is allowed to carry forward a net loss (negative taxable income as the net of revenue less deductions for costs, expenses and losses) in a tax year to use as a deduction in the succeeding seven years, as long as the company has the blue form tax return filing status. The blue form tax return filing status is given to a company filing requirements prescribed by the corporation tax law for keeping records of transactions, having obtained the permission by the Director of the District Tax Office and having filed its tax return every year on a timely basis.

LOCAL TAXES

A company is liable to pay local taxes on its income in addition to the corporation tax paid to the national government. Currently, local taxes applicable to a company are prefectural and municipal inhabitant taxes, enterprise tax and special local corporation tax.

CORPORATION TAX RATES

Corporations are taxed at a rate of 30%. A special reduced rate of 22% (19% for the tax years ending 1 April 2009–31 March 2012) is applicable for taxable income up to JPY 8 million of a small or medium-sized company.

TABLE 7

Corporate income tax rates

COMPANY SIZE	TAX RATE BEFORE 1 APRIL 2012	TAX RATE AFTER 1 APRIL 2012
Small & medium-sized enterprises (SMEs)		
• Up to JPY 8 million	22%	15%
• Over JPY 8 million	30%	25.5%
Large companies	30%	25.5%

A small and medium-sized company eligible for the special reduced rate is a company whose paid-in capital is JPY 100 million or less and is not 100% owned directly or indirectly by a company whose paid-in capital is JPY 500 million or more. Large companies are those whose paid-in capital is more than JPY 100 million.

According to a tax update of 2012, the basic rate of corporation tax will be reduced to 25.5% for tax years beginning on or after 1 April 2012. The special reduced tax rate will be lowered to 15% for tax years from 1 April 2012–March 2015.

LOCAL TAX RATES

Prefectural and municipal inhabitant taxes are calculated based on the amount of national corporation tax of a company. Applicable tax rates, which are determined respectively by a prefecture and a municipality, vary between standard and maximum rates.

TABLE 8

Prefectural and municipal inhabitant tax rates applied to national corporation tax amount

	STANDARD RATE	MAXIMUM RATE
Prefecture	5%	6%
Municipality	12.3%	14.7%
Total	17.3%	20.7%

In addition to taxes which are applied to a corporation's tax amount, a company is also liable to pay per capita inhabitant taxes to prefectures and municipalities, which are based on the amount of paid-in capital and the number of employees.

TAX RATES OF ENTERPRISE TAX

Enterprise tax, imposed by prefectures, is calculated based on the amount of a company's taxable income. Applicable tax rates determined by each prefecture vary between a standard and maximum rate.

TABLE 9

Enterprise tax rates

ANNUAL TAXABLE INCOME	PAID-IN CAPITAL <100 MILLION (JPY)		PAID-IN CAPITAL >100 MILLION (JPY)	
	STANDARD RATE	MAXIMUM RATE	STANDARD RATE	MAXIMUM RATE
Up to JPY 4 million	2.7%	3.24%	1.5%	1.8%
JPY 4 – 8 million	4.0%	4.80%	2.2%	2.64%
More than JPY 8 million	5.3%	6.36%	2.9%	3.48%

BUSINESS SCALE TAXATION (*GAIKEI HYOJUN KAZEI*)

As of 1 October 2008, business scale taxation has been imposed by prefectures as a special local enterprise tax. It is calculated based on the amount of taxable income multiplied by the standard rate of enterprise tax. Tax rates are as follows.

TABLE 10

Tax rates for business scale taxation

PAID-IN CAPITAL <100 MILLION (JPY)	PAID-IN CAPITAL >100 MILLION (JPY)
81%	148%

Please note: Business scale taxation was introduced as a temporary measure to adjust inequality in tax revenue among local governments. The tax rates shown in the table are the temporarily reduced rates which were revised corresponding to the introduction of business scale taxation.

EFFECTIVE TAX RATE

Enterprise tax and special local corporation tax are deductible in the calculation of taxable income for corporation tax. Taking into account the deductible nature of these local taxes, the effective tax rate is calculated as 40.83% for a company whose paid-in capital is more than JPY 100 million, assuming the maximum rates of inhabitant tax and enterprise tax are used in the calculation.

According to the tax update of 2012, the resulting effective corporate income tax rate for companies subject to the reduced rate of 25.5% is approximately 37%.

Under business scale taxation (*Gaikei Hyojun Kazei*), for certain corporations the effective tax rate is reduced to approximately 36%.

In addition, in order to assist reconstruction of Japanese companies, a special additional national corporation tax (10% of the normal corporation tax due) is imposed for three tax years beginning on or after 1 April 2012 under the special law to secure funds for reconstruction after the 11 March disaster.

OTHER TAXES

BUSINESS OFFICE TAX

Companies whose business premises exceed 1,000 square meters and/or employ in excess of 100 employees in designated cities are subject to business office tax. Designated cities have discretion whether or not to charge the tax.

FIXED ASSETS TAX

Real property and tangible depreciable fixed assets are subject to fixed asset taxes at the standard rate of 1.4%.

GROUP TAXATION REGIME

Under the 2010 tax reform, the Group Taxation Regime was introduced. It is the most important revision for Japanese subsidiary companies and Japanese branch offices of foreign companies. Group taxation is designed to reduce the negative effect the separate existence of related companies has on the aggregate tax liability of the group. Group taxation provides business groups flexibility to organise their business activities, internal restructurings and asset transfers.

Generally, the rules eliminate income and loss recognition on intra-group transactions by providing for deferral. The Group Taxation Regime automatically applies to certain transactions carried out by companies belonging to the same 100% group (companies with a 100% shareholding relationship directly or indirectly).

The main points of the Group Taxation Regime are:

- Capital gains/losses arising from transfers of assets between Japanese companies in a 100% group are deferrable
- The Dividends Received Deduction (DRD) – dividends from wholly-owned companies (100% Japanese subsidiaries) are exempt from taxable income without deducting attributable interest expense on such dividends
- Tax qualified dividends-in-kind between Japanese companies in a 100% group – dividends-in-kind are assets which companies distribute as dividends other than money. Dividends-in-kind between Japanese companies in a 100% group are treated as tax qualified dividends-in-kind. Recognition of capital gains/losses from tax qualified dividends-in-kind is deferred. In addition, withholding taxes are not imposed
- Donations between Japanese companies in a 100% group – a donation between Japanese companies in a 100% group is not deductible for the donating company. For the recipient company, the donation amount is not included in its taxable income.

Special tax reliefs are applied to small and medium-sized companies.

CONSOLIDATED TAX REGIME

A Japanese 100% group can choose the consolidated filing of income tax returns. Once a 100% group adopts consolidated filing, it is irrevocable unless specific events, such as change of ownership, occur. The consolidated tax return filing system is applicable only to Japanese companies in a 100% group, not to foreign companies.

The main benefit provided by the consolidated tax regime is the offsetting of profits and losses; a consolidated group can offset profits and losses within the group companies for national corporate tax purposes. However, some features of the consolidated tax regime may result in a tax burden. When a tax consolidated group forms or a subsidiary joins an existing consolidated group, assets of the subsidiaries will be re-evaluated at market value. These built-in gains/losses could result in additional taxation. In addition, tax losses incurred by the subsidiary before joining the consolidated group will be erased.

The consolidated tax return filing system is applied only to national corporate income tax. Local corporate income taxes are imposed on member companies. Each member company has to continue to pay local corporate taxes on an individual basis although the amount payable will be affected by the existence of the consolidation.

WITHHOLDING TAX CREDITS

Withholding taxes are imposed on incomes such as interest and dividends. In general, withholding taxes are creditable against corporate tax. An excessive amount of withholding tax on a corporate tax liability (if any) is refundable.

FOREIGN TAX CREDITS

A Japanese company is allowed to claim tax credits for foreign corporation tax, including foreign local tax and withholding tax that are paid directly by the Japanese company. There is a certain limit on the amount of creditable foreign tax.

FOREIGN DIVIDEND EXCLUSION SYSTEM

Under the Foreign Dividend Exclusion System, 95% of dividends from foreign subsidiaries to a Japanese parent company are exempted from corporate income tax. To apply for the Foreign Dividend Exclusion, foreign subsidiaries have to meet two qualifications:

- Hold 25% of shares or more directly or indirectly
- Hold 25% of shares or more at least six months before the date on which the obligation to pay the dividends is determined.

The exclusion system does not apply to subsidiaries with less than 25% shareholdings.

TRANSFER PRICING

The operation of transfer pricing taxation needs to be properly managed, taking into consideration the fact that this taxation system is based on arm's length principles. For this reason, it shall be operated in accordance with the basic policies stated below:

- A close examination will be made to assess whether prices fixed for foreign-related transactions are equal to the normal prices fixed for uncontrolled transactions. Where any problem is found with transactions, efforts shall be made to collect information widely on the market and business for an appropriate assessment of the calculation method selected and comparable transaction, and adjustment for differences

- To ensure the predictability of the corporation and to realise proper and smooth enforcement of transfer pricing taxation, the advance pricing agreements (APA) process shall be conducted in cases where an APA request regarding the transfer pricing mechanism (TPM) is submitted by the corporation, based on the contents of a mutual agreement related to the APA request (if there is any such agreement)
- To solve international double taxation caused by transfer pricing taxation, it is important for the tax authorities of each country to share an understanding of transfer pricing. Therefore, an examination or APA review shall be conducted in an appropriate manner by referring to the OECD Transfer Pricing Guidelines as necessary.

CONSUMPTION TAX

Japanese consumption tax, similar to European value added tax (VAT), is applied at the rate of 5% to the majority of goods and services consumed in Japan, including imports of goods and services.

There are a number of exemptions, including the lease or sale of land, education, medical treatment and social welfare activities. Exports and certain specific services invoiced to non-residents are 0% rated.

Under the tax update for the 2012 Tax Reform, the consumption tax rate will be increased from the current 5% rate to 8%, and then to 10% (8% will apply from 1 April 2014, with 10% applying from 1 October 2015). The tax exemption status for newly established SMEs will not be applicable to a subsidiary of a large corporation where such a subsidiary is established on or after 1 April 2014.

REGISTRATION

Vendors/service suppliers must register as consumption tax payers if they have taxable sales transactions in excess of JPY 10 million in the base period (two years before the current year). If the taxable sale in the base period is not more than JPY 10 million, the vendor/service supplier is able to elect whether or not they are treated as a consumption tax payer.

INCOME TAXES ON INDIVIDUALS

RESIDENT/NON-RESIDENT STATUS

Individuals are generally classified according to the period of their residence in Japan.

TABLE 11

Residency status

PERIOD OF RESIDENCE	STATUS
Up to 12 months	Non-resident
12 – 60 months	Non-permanent resident
More than 60 months	Permanent resident

Non-resident taxpayers are considered taxable on only their Japanese source income. Non-permanent resident taxpayers are taxable both on Japanese source income and part of the non-Japanese source income that is paid in and/or remitted to Japan. Permanent resident taxpayers are taxable on their worldwide income.

NATIONAL INCOME TAX AND LOCAL INHABITANT TAX

Individual taxes consist of national income tax and local inhabitant tax. The tax year is the calendar year beginning on 1 January. For local inhabitant tax, taxable income is based on the previous tax year's income.

NATIONAL INCOME TAX

The rate of tax levied on an individual is determined by the individuals' taxable income. As income increases, the marginal rate of tax increases. When calculating the net ordinary taxable income, a number of tax deductions are allowed, reducing taxable income.

Tax deductions available for individuals include, but are not limited to:

- Social insurance premiums paid to the Japanese government
- Life insurance premiums
- Earthquake insurance premiums
- Charitable contributions
- Qualified medical expenses
- Deductions for dependents (dependent spouse, children under 23 years old)
- Deduction for the elderly
- Deduction for the disabled.

TABLE 12

Individual tax rates – applied to the net of ordinary taxable income

NET TAXABLE ORDINARY INCOME (JPY)	TAX RATE	DEDUCTION (JPY)
0 – 1,950,000	5%	-
1,950,000 – 3,300,000	10%	97,500
3,300,000 – 6,950,000	20%	427,500
6,950,000 – 9,000,000	23%	636,000
9,000,000 – 18,000,000	33%	1,536,000
More than 18,000,000	40%	2,796,000

Calculation: taxable income × tax rate – deduction

LOCAL INHABITANT TAX

Local inhabitant tax consists of an 'income-based levy' and 'per-capita levy'. The tax rate of the income-based levy is 10% regardless of the amount of taxable income. As described above, taxable income for local inhabitant tax is based on the previous tax year's income. The amount of per capita levy is JPY 3,000 per capita for municipal inhabitant tax and JPY 1,000 for prefectural inhabitant tax.

CAPITAL GAINS

Capital gains from real estate realised by individuals are subject to tax separately from ordinary income and are classified as:

- Short-term capital gains (for real estate held less than five years) are taxable at a 30% income tax rate and a 9% inhabitant tax rate
- Long term capital gains (for real estate held more than five years) are taxable at a 15% income tax rate and 5% inhabitant tax rate.

In the case of the sale of the individual's residence, certain tax advantages are available (ie special deductions, loss carry-forward and a lower tax rate).

STAMP DUTY

Stamp duties are imposed on taxable documents, such as contracts and legal documents. They are imposed in the range of JYP 200–600,000.

IMPORTANT CHANGES 2011/2012 (FOR INFORMATION ONLY)

The new tax law has been updated to reflect the tax changes arising from the proposed 2011 Tax Reform Act, as well as the special legislation promulgated to cope with the aftermath of the great eastern Japan earthquake in March 2011.

The Law to Revise the Income Tax etc., in Order to Develop a Tax System to Address the Current Severe Economic Circumstances and Employment Conditions, Law No. 82 of 2011, consists of fast-track legislative items taken from the originally proposed 2011 Tax Reform Act submitted to the Diet on 25 January 2011. Tax changes include:

- Tax incentives for promoting comprehensive international strategic investment zones
- Tax incentives for designated multinational corporation research and development promotion enterprises
- Tax credits for corporations filing a blue tax return which increase employment during the year
- Clarification that a company may not be treated as a medium or small-sized company if it is owned 100% by more than one large-sized company within a 100% corporate group.

The Law to Revise the Income Tax etc., in Order to Construct a Tax System Addressing Changes in the Socio-Economic Structure, approved by the Japanese House of Representatives on 10 June 2011 consists of the remaining items from the original 2011 Proposed Tax Reform Act. This Tax Reform Act proposed reductions of the corporate tax rate and an increase of the consumption tax rate. Inheritance tax and gift tax are also to be revised by this ACT.

The Special Tax Law for those Affected by the Great Eastern Japan Earthquake, Law No. 29 of 2011, aims to help taxpayers affected by the earthquake. Relief measures include:

- Deduction of losses resulting from the earthquake from income for the 2010 tax year
- Increased deductibility and special credit for earthquake-related donations
- Additional first year depreciation for replacement property for property damaged or destroyed due to the earthquake
- Deferred gain treatment on replacement of property and business assets affected by the earthquake
- Carry back of losses arising from the earthquake.

In addition, under the tax update for 2012 Tax Reform, the period for tax loss carried forwards is extended from seven to nine years, while deductible amounts for large companies will be reduced from 100% of taxable income to 80%.

TAXATION OVERVIEW FOR NEW INVESTORS

The following section provides a taxation comparison overview for new foreign investors.

TAXABLE INCOME

SCOPE OF TAXABLE INCOME OF A CORPORATION

While domestic and foreign source income is subject to a corporate tax, a foreign tax credit is allowed to a corporation.

SCOPE OF TAXABLE INCOME OF A BRANCH

Only domestic source income is subject to corporate tax. No foreign tax credit is allowed for a foreign company.

A foreign company having a permanent establishment (PE) is subject to tax on all domestic source income or domestic source income attributable to the permanent establishment based on a tax treaty and must file a tax return. The remittance of funds from a Japanese branch to its foreign head office and transactions between them is generally not subject to corporate taxation.

It should be noted that by definition of PE of a foreign company, the treatment of business income, the location of source of income and taxation should be considered according to each tax treaty that may be in effect.

REPRESENTATIVE OFFICE

A representative office of a foreign company engaged in advertising, information provision, market survey, basic research and other supplementary activities in Japan for its head office is not subject to corporate tax.

TABLE 13

Notification to tax office regarding setting up a subsidiary

TIMING	NATIONAL TAX OFFICE	LOCAL TAX OFFICE
A	Notification of establishment of office paying salaries for withholding tax purposes	Notification of incorporation. Establishment of a company
B	Notification of incorporation of a company	
C	Application of Blue Return Filers	

TABLE 14

Notification to tax office regarding setting up a branch

TIMING	NATIONAL TAX OFFICE	LOCAL TAX OFFICE
*	Notification of establishment of office paying salaries for withholding tax purposes	Notification of incorporation. Establishment of a company
*	Notification of a foreign company with attachment	
*	Application of Blue Form Return	

* No particular deadline is regulated but it should be submitted at the latest within two months after the above matters are completed.

7 – ACCOUNTING & REPORTING

The Corporate Law amended in 2005 regulates accounting and reporting requirements for all companies in Japan.

This law requires that every company should maintain accurate records and prepare the following statements for each fiscal year:

- Balance sheet
- Income statement
- Statement of changes in net assets
- Annotations for the above statements
- Business report
- Supporting schedules.

Publicly listed companies are also governed by the Financial Instruments and Exchange Law. This law requires listed companies to prepare both financial statements and internal control reports. Therefore, listed companies have to comply with two laws for disclosure; the disclosures required by the Corporate Law are for shareholders, while the disclosures required by the Financial Instruments and Exchange Law are for investors. Both disclosures are similar, but the Financial Instruments and Exchange Law requires listed companies to provide further information, such as cash flow statements. For non-listed companies, only disclosures for the shareholders are required.

ACCOUNTING STANDARDS

Financial statements must be prepared in accordance with Generally Accepted Accounting Principles in Japan (J-GAAP).

J-GAAP is determined by the Financial Service Agency (FSA) and Accounting Standards Board of Japan (ASBJ). In some cases, foreign accounting standards such as the United States Generally Accepted Accounting Principles (US-GAAP) or International Financial Reporting Standards (IFRS) can be used for preparation of financial statements. IFRS usage has been voluntary in Japan since 2009 (fiscal year). J-GAAP is equivalent to IFRS, though some differences will remain until reviews of IFRS have been completed.

The FSA and the ASBJ have been taking major steps to secure the convergence of J-GAAP with IFRS. In 2009, the FSA announced that the mandatory implementation of IFRS for listed companies would be in 2015/16 if a decision was finalised in 2012. The FSA also announced that the mandatory implementation of IFRS would only be on consolidated financial statements of listed companies. J-GAAP would continue to be applied for non-listed companies' financial statements and stand-alone financial statements for listed companies.

In June 2011, the FSA decided that the mandatory transition to IFRS will be extended from the current minimum of three years to 5–7 years due to resistance in the business community, which is labouring to recover from the Great East Japan Earthquake of March 2011.

AUDIT

The Japanese Corporate Law requires large companies' annual accounts to include a report from a suitably qualified and registered auditor to the shareholders. Qualified auditors are certified public accountants (CPA) or auditing firms registered in Japan. The law stipulates that a large company is a company whose capital stock exceeds JPY 500 million or whose total amount of liabilities (as of the latest balance sheet date) exceeds JPY 20 billion. The Financial Instruments and Exchange Law also requires listed companies to have their financial statements audited by a qualified auditor.

ACCOUNTING AND REPORTING REQUIREMENTS FOR BRANCHES

A foreign company with a Japanese branch must attach the financial statements of the Japanese branch, as well as those of the company as a whole, to the Japanese corporate tax return to be filed each fiscal year.

A foreign company conducting regulated business (ie banking or insurance) must prepare financial statements for the government in compliance with the relevant laws governing such regulated business. There are no extra accounting and reporting requirements applicable to a branch that conducts non-regulated businesses.

8 – UHY REPRESENTATION IN JAPAN

UHY TOKYO & CO. JAPAN

CONTACT DETAILS

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www.uhy-tokyo.or.jp

CONTACTS

Liaison contact: Nobuyuki Hara
Position: Managing Partner
Email: info@uhy-tokyo.or.jp

Year established: 1984
Number of partners: 13
Total staff: 41

OTHER IN-COUNTRY OFFICE LOCATIONS AND CONTACTS

Kyoto

BRIEF DESCRIPTION OF FIRM

UHY Tokyo & Co is proud of its lengthy and strong client relationships with a range of major listed companies in Japan, founded on our excellent audit capabilities and management relationships. With our close support and range of capabilities, several of our clients have grown from small venture companies to major leaders in their respective fields.

Our experienced specialists in International Financial Reporting Standards (IFRS) provide clients with useful guides to meeting the new standards. Our IT specialists have significant experience in IT networks. In addition, our skills and manpower are able to meet whatever requirements or challenges existing and potential clients may have for international business expansion.

What helps to make UHY Tokyo & Co unique among mid-level audit firms are our depth of experience and English-language capabilities, a combination rarely found among our competitors. Our reputation and professional standing have been built on service excellence and pride in our work. Our clients agree.

SERVICE AREAS

Audit and assurance
Statutory Audit
Contractual Audit
IFRS Standards
Internal Control and Risk Management
Information System Audit
Organisation Audit
Risk Audit
Business Advisory Service
Accounting Systems
Tax Advisory Service
Global Taxation
Corporate Taxation

The network for doing business

Individual Taxation
Due diligence
Investigation and evaluations
Mergers and acquisitions
Business and strategic planning

PRINCIPAL OPERATING SECTORS

Retailing
Manufacturing
IT services
Service
Transportation
Finance
Fund
Financial Services
Consulting Services

LANGUAGES

Japanese and English.

CURRENT PRINCIPAL CLIENTS

Partial list of clients permitting public disclosure:
Universal Entertainment Corporation
Don Quijote Co., Ltd
Nagasakiya Co., Ltd
OM2 Network Co., Ltd
Accretive Co., Ltd
SADAMATSU Company Limited
GaiaX Co. Ltd.
ACMOS INC.
GOKURAKUYU Co., Ltd
CIMA Co., Ltd
ThreePro Group Inc.
SHINWA ART AUCTION CO.,LTD.

OTHER COUNTRIES IN UHY CURRENTLY WORKING WITH, OR HAVE WORKED WITH IN THE PAST

USA,Vietnum,Korea,Hongkong

BRIEF HISTORY OF FIRM

Originally established in April 1984 as ‘San-Ei & Co’, we became ‘BA Tokyo & Co’ several years later, choosing ‘BA’ to mean ‘Business Assurance’ to our clients.

The firm was a member of the Mazars network from May 2002 until October 2010.

We established Kyoto and Okutama offices to continue to meet the needs of our clients in Japan and our growth over the years has led us to become one of Japan's leading mid-size audit corporations with considerable experience in a variety of sectors.

In 2009 our firm organised three product groups to provide a new range of high quality services to meet client needs: IFRS+US GAAP PG; IT internal control PG; and Tax+fraud PG.

The firm joined UHY in 2011 and changed firm name to UHY Tokyo & Co from BA Tokyo & Co.

In 2012 we closed Okutama office.

LET US HELP YOU ACHIEVE FURTHER BUSINESS SUCCESS

To find out how UHY can assist your business, contact any of our member firms. You can visit us online at www.uhy.com to find contact details for all of our offices, or email us at info@uhy.com for further information.