

Japan

Corporate Taxation 2008

Contents

	Page
1. Jurisdiction	2
2. Major taxes on corporations	2
3. Organisations taxable as corporations	5
4. Taxable income of resident corporations	6
5. Taxation of non-resident corporations	7
6. Liquidations	8
7. Reorganisations	8
8. Taxation of shareholders (corporations and individuals)	9
9. Returns	10
10. Investment incentives	10
11. Other significant taxes	11
12. Tax treaties and withholding tax rates	12
13. Corporate tax calculation	14

1. Jurisdiction

(1) Scope of Japan's Corporate Tax

A corporation with its head office in Japan is considered a domestic corporation, and is subject to Japanese corporate income taxes on its worldwide income including capital gains.

A foreign corporation is subject to Japanese corporate income taxes on all its income and capital gains from Japanese sources. A foreign corporation with a Japanese branch may also be subject to Japanese corporate income taxes on Japanese source income attributable to the branch.

2. Major taxes on corporations

(1) National Tax

A domestic corporation is subject to corporation tax at the following rates:

① Annual Taxable Income Bracket

Company with capital	Annual taxable income bracket	Applicable tax rate
(A) 100 million yen or less:	0 - 8 million yen	22 %
	Over 8 million yen	30 %
(B) Over 100 million yen :	All income	30 %

(2) Local Taxes

Local taxes consist of prefectural and municipal inhabitant taxes and enterprise tax.

① Inhabitant Taxes

Inhabitant taxes are computed as a percentage of the corporation tax within the range shown below.

Prefecture	5.0% - 6.0%
Municipal	12.3% - 14.7%
Tokyo Metropolitan	17.3% - 20.7%

In addition to the above income tax, the following per capita taxes are assessed.

Paid-in Capital (Unit: million yen)	Numbers of employees	
	50 or less (Unit: thousand yen)	More than 50
0 - 10	70	140
10 - 100	180	200
100 - 1,000	290	530
1,000 - 5,000	950	2,290
Over 5,000	1,210	3,800

② Enterprise Tax

(a) Tax Rate

Enterprise tax is computed as a percentage of taxable income at the following rates:

Annual taxable Income bracket* (Unit: million yen)	Applicable tax rate (%)	From October 1st 2008***
0 - 4	5.0 - 6.00**	2.7 - 2.95%
4 - 8	7.3 - 8.76	4.0 - 4.365%
Over 8	9.6 - 11.52	5.3 - 5.78%

*The benefit of the lower rates for the small income bracket is not applicable to a corporation with paid-in capital of 10 million yen or more which has places of business in three prefectures or more.

** Local governments are authorized to raise the tax rates up to 1.2 times the above standard rates.

*** This will be in addition to a newly introduced national tax.

As shown in the chart above, for fiscal years starting on or after 1 October 2008 the rates will be revised. Additionally, a national component will be added which will be calculated based on the amount calculated under the new rates. The revisions will not result in a significant change in the tax amount for corporate taxpayers.

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(b) New Enterprise Tax

For fiscal years beginning on or after 1 April 2004, Enterprise Tax for companies with share capital of over 100 million yen is instead calculated as the sum of an income-based, a value added-based, and capital-based component.

a. Income-based component:

Annual taxable income bracket (Union: million yen)	Current rate (%)*	From October 1st 2008**
0 - 4	3.80 - 4.56	1.5 - 1.69%
4 - 8	5.50 - 6.60	2.2 - 2.475%
Over 8	7.20 - 8.64	2.9 - 3.26%

* Local governments are authorized to raise the tax rates up to 1.2 times the minimum rates.

** This will be in addition to a newly introduced national tax.

Similar to the changes shown in the previous section for corporations with capital of 100 million yen or less, the rate changes for fiscal years starting on or after 1 October 2008 are in addition to a newly added national component that is calculated based on the income-based amount under the new rates. The revisions will not result in a significant change in the tax burden.

b. Value added-based component:

Value added-based component = Value added x 0.48%

The standard rate of 0.48% is imposed on the taxable base of value added calculated according to the following formula:

Value added = Annual taxable income (before deduction of tax loss carry forward) + Profit distributed *

* Profit distributed is the total amount of salary, net interest payment, and a net rent payment. Salary means remuneration, salary, wages, bonuses, and retirement allowance and includes 75% of labour outsourcing contract fees. If the total of the salary amount exceeds 70% of the profit distributed, the excess is deducted from the profit distributed.

c. Capital-based component:

Capital-based component = Capital amount x 0.2%

The capital-based component is the capital amount (the total amount of the share capital and capital reserve) multiplied by the standard rate of 0.2%. Special treatments may apply for the following cases:

- In case of holding companies, the amount corresponding to the book value of the capital of the subsidiaries is deducted from the capital amount.
- If a company's capital exceeds 100 billion yen, the following amount is assumed as the capital amount in the calculation of the tax base. If the capital amount exceeds 1,000 billion yen, the capital amount is assumed to be 1,000 billion yen for tax purposes.

Capital amount = (i) + (ii) + (iii)

(i). 100 billion yen

(ii). (Amount exceeding 100 billion yen up to 500 billion yen) x 50%

(iii). (Amount exceeding 500 billion yen up to 1,000 billion yen) x 25%

(3) Total Tax Rate

The maximum Corporation Tax rates are:

① In case of companies with share capital of 100 million yen or less

	Applicable tax rate (%)
Corporation tax	30.00
Inhabitant tax (20.7% of corporation tax)	6.21 (30% x 20.7%)
Enterprise tax	11.52
Total surface rate	47.73
Effective tax rate*	42.79

② In case of companies with share capital of over 100 million yen

	Applicable tax rate(%)
Corporation tax	30.00
Inhabitant tax (20.7% of corporation tax)	6.21 (30% x 20.7%)
Enterprise tax	8.64
Total surface rate	44.85
Effective tax rate*	41.28

* The effective tax rate is calculated by dividing the total surface rate by 1.1152 or 1.0864 taking into consideration an available deduction of enterprise tax for both corporation tax and enterprise tax purposes when paid or in the following year irrespective of payment.

(4) Additional Tax on Undistributed Profit of Family Corporations

If 50% or more of the total issued shares of a domestic corporation are directly or indirectly owned by an individual shareholder together with his or her relatives, the corporation is considered a Family Corporation. A Family Corporation is subject to an additional corporation tax at the following rates on undistributed profit for any accounting period in excess of a designated amount (minimum 15 million). For fiscal years beginning on or after 1 April 2007, Family Corporations with share capital of 100 million or less are not subject to this additional tax.

Annual Undistributed Profit Bracket (Unit: million yen)	Applicable tax rate (%)
0 - 30	10
30 - 100	15
Over 100	20
An additional inhabitant tax is assessed at rates shown above.	No additional enterprise tax is assessed.

3. Organisations taxable as corporations

(1) Principal forms of business entities subject to corporate income taxation

Principal Forms of Business Entities Subject to Corporate Income Taxation

- ① A limited stock company - Kabushiki Kaisha
- ② A company of members with both limited and unlimited liability - Goshi Kaisha, Chukan Hojin
- ③ A company of members with unlimited liability - Gomei Kaisha
- ④ A limited liability company - Goudou Kaisha

A general partnership (Kumiai) is a pass-through entity, therefore it is not subject to corporate income taxation. Each item of a partnership's income or gain is allocated to partners and is subject to income taxation at partner level.

The net income or loss of a silent partnership (Tokumei Kumiai) allocated to its partners under the partnership agreement is excluded from the operator's taxable income or loss, and the amount allocated to partners is included in the partner's taxable income or loss.

4. Taxable income of resident corporations

(1) The Tax Base

Taxable income is the net amount of gross income less deductions and is derived from net income computed in accordance with generally accepted accounting principles after additions and deductions of certain items of non-deductible expenses and excluding income in accordance with the tax law. Depreciation and amortisation, valuation loss and provision for various reserves must be entered in the books of account in order for them to be deductible for tax purposes.

(2) Dividends Received

Dividends received from a Japanese corporation are excluded from taxable income. If an investor corporation owns 25% or more of the shares of a corporation for a consecutive period of 6 months or more before declaration of the dividends, 100% of the dividends received are excluded from taxable income. Otherwise, 50% of the dividends are excluded from taxable income. The amount of dividends received exclusion is reduced by the interest cost allocated to investments producing dividends.

(3) Depreciation

Japanese tax laws allow for depreciation on both tangible and intangible assets, excluding land costs.

The depreciable basis of fixed assets is the purchase price, or market price in the case of assets acquired as a gift, or total cost in the case of assets constructed by the corporation. A company may select either the straight-line method or declining-balance method for each asset or groups of assets. The straight-line method is used mainly for intangible assets. Buildings, however, may only be depreciated by using the straight-line method.

Useful lives of depreciable assets as determined by the Ministry of Finance

	Years
Reinforced concrete buildings (office-use)	50
Wooden buildings (office-use)	24
Air-conditioning equipment	6
Personal Computers (excluding servers)	4
Cars	6

In addition to regular depreciation, special depreciation is permitted.

(4) Net Operating Loss

A tax loss may be carried forward for 7 years (For business years beginning on or before March 31, 2001 5 years). A tax loss may be carried back one year only for corporation tax. The 1992 Tax Reform suspended carry-back of net operating loss for the accounting periods ended between 1 April, 1992 and 31 March, 2010, except for losses incurred in the accounting period of the dissolution of a corporation.

(5) Charges by Parent

Charges made by a foreign parent are deductible to the extent that such charges are made on an arm's-length basis.

(6) Foreign Taxes

With certain limits, a domestic corporation may claim a foreign tax credit against corporation tax and inhabitant tax. Unused foreign tax credits may be carried forward for 3 years.

(7) Thin Capitalisation Rule

Thin capitalisation rule limits the tax deductibility of interest paid to foreign controlling shareholders.

If the average total debt balance of a domestic corporation exceeds 3 times net equity and if the average balance of the debt to the foreign controlling shareholder exceeds 3 times the foreign controlling shareholder's equity in the net assets of the domestic corporation, the amount of interest on the exceeding debt to the foreign controlling shareholder is not deductible.

Foreign controlling shareholders are non-resident individuals or foreign corporations which own, directly or indirectly, 50% or more of the outstanding shares of the domestic corporation, or which have special relations provided in the regulations with the domestic corporation. Similar rules apply to interest which is deductible against the profit of the Japanese Branch of a foreign corporation.

(8) Other Items

Deduction of entertainment expenses for tax purposes is subject to special limitations as follows:

Paid-in capital amount (Unit: million yen)	Statutory limit (annual) (Unit: million yen)
Less 100	4
100 or more	0

In addition, 10% of the entertainment expense up to the statutory limit is not deductible.

5. Taxation of non-resident corporations

(1) Taxation of Registered Branch or Other Permanent Establishment

A foreign corporation is taxable on the income and gains of its Japanese branch or other permanent establishment in the same way as a Japanese corporation. However, no withholding tax applies to profits remitted by the branch.

(2) Taxation at Source of Investment Income Paid to Non-residents

Unless otherwise provided by tax treaty, dividends, interest, rent and royalties paid by a Japanese corporation to non-residents (both corporate and individuals) are subject to withholding tax of 20%

6. Liquidations

(1) Taxation of Liquidation Income

Where a domestic corporation is legally dissolved (for liquidation or by merger), a tax on liquidation income replaces the usual corporate income tax.

When liquidation occurs during a business year, ordinary income tax is levied up to the date of dissolution.

The liquidation income of a corporation is the excess of its residual assets distributable to shareholders over the sum of its capital stock, paid-in surplus and accumulated earnings at the time of dissolution.

The corporation tax rate of liquidation income is 27.1%. Inhabitant tax and Enterprise tax are also assessed on liquidation income.

(2) Taxation of Shareholders

Shareholders of a liquidated corporation are subject to tax for deemed dividend income (distribution out of accumulated profit of the liquidated corporation), if any.

7. Reorganisations

For tax purposes, there are both qualified and nonqualified reorganizations. In a qualified reorganization, transferor corporations do not recognize any gains or losses and transferee corporations carry over the basis in the assets and liabilities of the transferor. Shareholders in a qualified reorganization do not recognize any gains or losses for the exchange of the shares in the transferor corporation for the shares in the transferee corporation. Certain conditions must be satisfied for a reorganization to be qualified.

(1) Mergers

The successor corporation must file a return and pay tax on the liquidation income of the absorbed corporation within two months after the merger. The tax rate is the same as for liquidations.

(2) Other Forms of Reorganisation

A corporation is not treated as dissolved if it changes its organisation in accordance with the laws or regulations but remains substantially unchanged.

8. Taxation of shareholders (corporations and individuals)

(1) Taxation at Source of Investment Income Paid to Non-residents

Dividends, interest, rent, and royalties paid by a Japanese corporation to non-residents are subject to withholding tax at 20% (15% in case of interest on bank deposits and certain debt securities). Reduced rates may be available under an applicable tax treaty.

(2) Capital Gains Realised by Non-residents

① Shares

Capital gains realised by a non-resident corporation or a non-resident individual on sales or disposition of shares are not subject to tax unless the sales are made systematically or the shareholder owing 25% or more of the shares at any time in the preceding 3 year period sold 5% or more of the shares in the current fiscal year.

Taxable capital gains on the sale of shares etc. by a non-resident individual are subject to 20% income tax separately from other income.

② Japan Real Property

If a non-resident corporation or individual transfers land, rights to land, a building or annex, or a structure situated in Japan, the transferee, whether a resident or a non-resident and whether a domestic or a foreign corporation, is required to withhold 10% of the value of the transfer and pay the amount to the Japanese Government. A gain from the sale or other transfer of Japan real property is subject to Japanese income tax. The 10% withholding income tax may be credited against tax on the capital gain.

③ Taxation of Domestic Shareholders of Foreign Corporations

Dividends paid by a foreign corporation to Japanese shareholder corporations are taxed at normal income tax rates less any foreign tax credit. The exclusion of dividends from taxable income is not applicable to dividends paid by a foreign corporation (compare with domestic corporations at 4(2) above). Related capital gains are taxed as ordinary income.

9. Returns

(1) Taxable Period and Filing Requirement

The taxable period generally means the accounting period stipulated in the company's articles of incorporation on the basis of which the taxpayer regularly prepares its financial statements. Accounting periods of 52 or 53 weeks are not allowed under Japanese laws. A corporation is required to file a final return within 2 months after the end of the accounting period, unless prior approval was obtained from the tax office for a one month or more extension. A corporation whose taxable period is longer than 6 months has to file an interim return within two months after the first 6 month period.

(2) Payment Dates and Advance Payments

The Japanese tax system is a self-assessment and payment system. Tax payments must be made no later than 2 months after the close of the accounting period covered by the return.

An advance payment of usually one half of the prior year's liability has to be made with the interim tax return. However, a corporation may elect to calculate the prepayment on the basis of the tax provisionally due on taxable income for the 6 month period.

(3) Additional Assessments

The period for additional assessments of income is normally 5 years (7 years in the case of fraud or tax evasion) from the end of the appropriate year.

10. Investment incentives

(1) Overseas Investment Loss Reserve

Tax-free reserves may be set up in respect of share investments in and long-term credit extended to certain foreign corporations in developing countries, etc up to 31 March, 2010. The permitted reserves range from 30% to 100% of acquisition cost of the shares. The reserves must be reversed to taxable income after a lapse of a 5 year period at the rate of 20% a year, i.e. for the following 5 years.

(2) Research and Development Tax Credit

A new tax credit for research and development expenses of up to 10% of corporate income tax due for the year was introduced in 2008. This is in addition to the gross based tax credit of 8% - 10% of research and development expenses that is capped at 20% of corporate income tax due for the year. The new credit is a temporary measure available for corporate fiscal years starting between April 1, 2008 and March 31, 2010.

(3) Human Resource Investment Tax Credit

This tax credit system allows a corporation that has increased its expenditure on employee training over the average training expenditure in the previous two years to credit the lesser of 25% of the increased amount or 10% of the corporation tax. The training expenditure includes payments for external instructors, training materials, accommodation for training, and fees for external training courses. This tax credit applies for three years from the business year starting on April 1, 2005.

11. Other significant taxes

(1) Turnover Tax

Transfer of assets, lease or rental of assets and rendering of services conducted by enterprises within the Japanese territory, and imports of tangible goods into Japan, are subject to 5% consumption tax. 1% out of 5% is allocated to local governments. Export sales are subject to consumption tax at zero rate.

(2) Social Security Tax

Social security contributions are based on payroll and cover health, welfare pension, workmen compensation and unemployment insurance. Employers pay approximately 50% of the premiums.

(3) Other Taxes

- Real property tax
- Automobile tax.
- Registration tax

12. Tax treaties and withholding tax rates

Tax treaties may modify the general principles of taxation described herein and have been concluded with countries listed in the table below.

Withholding Tax Rates				
Treaty Country	Royalties (%)	Interest (%)	Dividends	
			General (%)	Parent-Subsidiary (%)
Australia	10	10	15	15
Austria	10	10	20	10
Bangladesh	10	10	15	10
Belgium	10	10	15	10
Brazil	12.5/15/20	12.5	12.5	12.5
Bulgaria	10	10	15	10
Canada	10	10	15	5/10
China	10	10	10	10
Czech Republic	0/10	10	15	10
Denmark	10	10	15	10
Finland	10	10	15	10
France	10	10	15	0/5
Germany	10	10	15	10
Hungary	0/10	10	10	10
India	10	10	10	10
Indonesia	10	10	15	10
Ireland	10	10	15	10
Israel	10	10	15	5
Italy	10	10	15	10
Korea	10	10	15	5
Luxembourg	10	10	15	5
Malaysia	10	10	15	5
Mexico	10	10/15	15	0/5
Netherlands	10	10	15	10
New Zealand	0	0	15	15
Norway	10	10	15	5

Pakistan	0	30	15	15
Philippines	10/15/20	10/15	25	10
Poland	0/10	10	10	10
Romania	10/15	10	10	10
Russian Federation	0/10	10	15	15
Singapore	10	10	15	5
Slovak Republic	0/10	10	15	10
South Africa	10	10	15	5
Spain	10	10	15	10
Sri Lanka	0/50	0	20	20
Sweden	10	10	15	0/5
Switzerland	10	10	15	10
Thailand	15	10/25	15/20	15/20
Turkey	10	10/25	15/20	10/15
United Kingdom	0	10	10	0/5
United States	0	10	10	0/5
Vietnam	10	10	10	10
Zambia	10	10	0	0

Notes:

1. A rate of zero is generally applied to film royalties.
2. The tax treaty with Czechoslovakia is applicable between Czech Republic/Slovak Republic and Japan.
3. The Russian Federation includes Armenia, Belarus, Georgia, Kyrgystan, Moldova, Tajikistan, Turkmenistan, Ukraine, Uzbekistan.

13. Corporate tax calculation

Assumed facts (in thousands of Yen)

Taxable period (one year) ended: 31 March, 2008

Taxable income	40,000 yen
Dividends declared	5,000 yen
Retained income	35,000 yen
Paid-in capital	50,000 yen
Number of employees	40

Calculation of Corporate Tax of Japanese Corporation

(1) National Tax

Corporation tax

Taxable Amount	Tax Rate	Tax Payable
000 %		000 yen
8,000 x	22.0 =	1,760
32,000 x	30.0 =	9,600
40,000		11,360

(2) Local Tax

Enterprise tax

4,000 x	5.5 =	220
4,000 x	8.03 =	321
32,000 x	10.56 =	3,379
40,000		3,920

Inhabitant tax

11,360 x	20.7 =	2,351
Flat tax	=	180
		2,531

