

KPMG Japan Tax Newsletter

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OUTLINE OF THE 2022 TAX REFORM PROPOSALS

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The ruling coalition (the Liberal Democratic Party and Komeito) agreed on the 'Outline of the 2022 Tax Reform Proposals' (Proposal) on 10 December 2021. We have set out below brief summaries of the main points of the Proposal.

The Proposal itself is only an indicative outline and is unclear with respect to some of the contemplated changes. The details of the tax reform will be unveiled in the bills revising the tax laws and the succeeding amended tax laws, cabinet orders and ministerial ordinances. Please note that the final tax reform could differ from the Proposal depending on the outcome of discussions in the Diet.

I. Corporate Taxation

1. Tax Credits for Acceleration of Substantial Salary Increases

Where a blue-return filing company meets certain conditions such as sufficient salary increases (different conditions are provided for large-sized companies and small and medium-sized companies, respectively) for fiscal years beginning on or before 31 March 2023, tax credits based on the amount of the salary increase, etc. are allowed.

(1) Amendments to the measure for large-sized companies

By virtue of the 2022 tax reform, from the viewpoint of promoting substantial salary increases for each employee based on a long-term perspective and encouraging returns to various stakeholders including not only shareholders but also employees and business partners, the current measure will be fundamentally strengthened as follows:

[Current tax law]

Eligible period	Fiscal years beginning between 1 April 2021 and 31 March 2023	
Conditions	(i)	[Salary payments for newly hired employees in the current fiscal year] ≥ [Salary payments for newly hired employees in the preceding fiscal year] x 102%
	(ii)	[Education and training costs in the current fiscal year] ≥ [Education and training costs in the preceding fiscal year] x 120%
Tax credit (Upper limit: corporation tax liability x 20%)	Where only condition (i) is satisfied	[Salary payments for newly hired employees in the current fiscal year] x 15%
	Where conditions (i) and (ii) are satisfied	[Salary payments for newly hired employees in the current fiscal year] x 20%

[Proposal]

Eligible period	Fiscal years beginning between 1 April 2022 and 31 March 2024	
Conditions ^(*)	(i)	[Salary payments for continuously employed people in the current fiscal year] ≥ [Salary payments for continuously employed people in the preceding fiscal year] x 103%
	(ii)	[Salary payments for continuously employed people in the current fiscal year] ≥ [Salary payments for continuously employed people in the preceding fiscal year] x 104%
	(iii)	[Education and training costs in the current fiscal year] ≥ [Education and training costs in the preceding fiscal year] x 120%
Tax credit (Upper limit: corporation tax liability x 20%)	Where only condition (i) is satisfied	{[Salary payments in the current fiscal year] – [Salary payments in the preceding fiscal year]} x 15%
	Where condition (ii) is satisfied	{[Salary payments in the current fiscal year] – [Salary payments in the preceding fiscal year]} x 25%
	Where conditions (i) and (iii) are satisfied	{[Salary payments in the current fiscal year] – [Salary payments in the preceding fiscal year]} x 20%
	Where conditions (ii) and (iii) are satisfied	{[Salary payments in the current fiscal year] – [Salary payments in the preceding fiscal year]} x 30%

(*) For companies, whose number of regular employees is 1,000 or more, with stated capital of JPY1 billion or more, this measure will be applicable only when they have notified the Minister of Economy, Trade and Industry that they have made public announcement about the policy of salary increases, the policy of building appropriate relationships with business partners, and other matters through the internet.

In addition, under the current tax law, when applying the additional tax credit rate for education and training costs, it is necessary to attach documents describing the details of education and training costs to a final tax return, etc. By virtue of the 2022 tax reform, it is proposed that the retention of documents is sufficient to enable the application of the additional tax credit rate.

(2) Amendments to the measure for small and medium-sized companies

By virtue of the 2022 tax reform, from the viewpoint of promoting substantial salary increases and investment in human resources while protecting employment of small and medium-sized companies as a whole, the current measure will be amended as follows:

[Current tax law]

Eligible period	Fiscal years beginning between 1 April 2021 and 31 March 2023	
Conditions	(i)	[Salary payments in the current fiscal year] ≥ [Salary payments in the preceding fiscal year] × 101.5%
	(ii)	[Salary payments in the current fiscal year] ≥ [Salary payments in the preceding fiscal year] × 102.5%
	(iii)	Either (a) or (b) is met: (a) [Education and training costs in the current fiscal year] ≥ [Education and training costs in the preceding fiscal year] × 110% (b) The Business Plan for Improvement of Management Capability was approved by the competent minister under the Small and Medium-sized Enterprises Business Enhancement Act by the end of the fiscal year and the fact that the management capability was improved in accordance with the Business Plan was certified.
Tax credit (Upper limit: corporation tax liability × 20%)	Where only condition (i) is satisfied	{[Salary payments in the current fiscal year] – [Salary payments in the preceding fiscal year]} × 15%
	Where conditions (ii) and (iii) are satisfied	{[Salary payments in the current fiscal year] – [Salary payments in the preceding fiscal year]} × 25%

[Proposal]

Eligible period	Fiscal years beginning between 1 April 2022 and 31 March 2024	
Conditions	(i)	[Salary payments in the current fiscal year] ≥ [Salary payments in the preceding fiscal year] × 101.5%
	(ii)	[Salary payments in the current fiscal year] ≥ [Salary payments in the preceding fiscal year] × 102.5%
	(iii)	[Education and training costs in the current fiscal year] ≥ [Education and training costs in the preceding fiscal year] × 110%
Tax credit (Upper limit: corporation tax liability × 20%)	Where only condition (i) is satisfied	{[Salary payments in the current fiscal year] – [Salary payments in the preceding fiscal year]} × 15%
	Where condition (ii) is satisfied	{[Salary payments in the current fiscal year] – [Salary payments in the preceding fiscal year]} × 30%
	Where conditions (i) and (iii) are satisfied	{[Salary payments in the current fiscal year] – [Salary payments in the preceding fiscal year]} × 25%
	Where conditions (ii) and (iii) are satisfied	{[Salary payments in the current fiscal year] – [Salary payments in the preceding fiscal year]} × 40%

In addition, under the current tax law, when applying the additional tax credit rate for education and training costs, it is necessary to attach documents describing the details of education and training costs to a final tax return, etc. By virtue of the 2022 tax reform, it is proposed that the retention of documents is sufficient to enable the application of the additional tax credit rate.

[Definition of key terms]

- Large-sized companies: Companies other than small and medium-sized companies
- Small and medium-sized companies: (i) or (ii) below:
 - (i) Companies with stated capital of JPY100 million or less, except for the following cases:
 - at least 50 percent of the shares are held by one large-scale company (e.g. a company whose stated capital is over JPY100 million); or
 - at least two-thirds of the shares are held by two or more large-scale companies
 - (ii) Companies with no capital whose number of regular employees is 1,000 or less

Note that a company whose 'annual average income' is over JPY1.5 billion is excluded from the definition of small and medium-sized companies. 'Annual average income' is measured using income in the fiscal years ended during 3 years before the beginning date of the current fiscal year.

- Salary payments: Salary paid to domestic employees which is deductible in calculating the company's income for each fiscal year

- Domestic employees: Employees (excluding employees who have a special relationship with directors or who have the status of directors) working at offices located in Japan, who are listed in a wage ledger prescribed by the Labor Standards Act
- Newly hired employees: Domestic employees who have worked for a year or less since the start of working at a domestic office of a company
- Continuously employed people: Certain domestic employees who worked for the full period of the current fiscal year and the full period of the preceding fiscal year

2. Restriction on Eligible Companies for Special Tax Measures

Large-sized companies, which do not take positive actions for salary increases and capital investment in spite of increasing their profits, are restricted from certain types of special tax measures.

By virtue of the 2022 tax reform, this measure will be amended as follows:

[Current tax law]

(1) Outline of the measures	Large-sized companies are not allowed to apply tax credits under the five special tax measures indicated in (3) below for fiscal years beginning between 1 April 2018 and 31 March 2024 where neither condition (i) nor (ii) in (2) is met.		
(2) Conditions	Neither (i) nor (ii) is met:		
	(i)	(a) Salary payments for continuously employed people in the current fiscal year (If both (a) and (b) are zero, condition (i) is treated as being satisfied.)	(b) Salary payments for continuously employed people in the preceding fiscal year
	(ii)	Total acquisition costs of depreciable assets located in Japan in the current fiscal year	Total depreciation costs of depreciable assets recorded in the current fiscal year x 30%
	This rule is not applied for fiscal years where the current fiscal year's income is equal to or smaller than the preceding fiscal year's income.		
(3) Scope of special tax measures to be restricted	Tax credits under the following measures: <ul style="list-style-type: none"> • Tax credits for R&D costs • Special measures for promoting future investment in communities • Special measures for promoting investment in 5G technology • Special measures for promoting investment in digital transformation • Special measures for promoting investment for carbon neutrality 		

[Proposal]

For the following target companies, the condition (i) in (2) above will be strengthened as follows:

Target company	Companies which fall under both of the following: <ul style="list-style-type: none"> The stated capital is JPY1 billion or more and the number of regular employees is 1,000 or more Certain cases ^(*) where income in the preceding fiscal year exceeds zero 		
Condition (i) in (2) above	Fiscal years beginning between 1 April 2022 and 31 March 2023	Salary payments for continuously employed people in the current fiscal year	> Salary payments for continuously employed people in the preceding fiscal year $\times 100.5\%$
	Fiscal years beginning between 1 April 2023 and 31 March 2024	Salary payments for continuously employed people in the current fiscal year	> Salary payments for continuously employed people in the preceding fiscal year $\times 101\%$

^(*) Certain cases include the case where the current fiscal year includes the date of establishment or merger, etc.

[Definition of key terms]

- Total acquisition costs of depreciable assets located in Japan: Total acquisition costs of the depreciable assets (limited to buildings and facilities attached to buildings, structures, machinery, ships, aircraft, vehicles and delivery equipment, tools, furniture and fixtures, certain intangible fixed assets and certain animals) among assets (except for inventories, securities and deferred assets) in use for business in Japan and acquired in the current fiscal year and owned by a company at the end of the current fiscal year
- Total depreciation costs of depreciable assets recorded in the current fiscal year: Total depreciation costs of depreciable assets owned by a company and recorded as expenses in the books of account (the amount of excess depreciation in the preceding fiscal year is excluded and the amount recognized as a special reserve is included.)

(Please refer to [Definition of key terms] in '1. Tax Credits for Acceleration of Substantial Salary Increases' for other terms.)

3. Japanese Group Relief System

(1) Amendments to tax book value adjustment method

The Japanese Group Relief System (JGR) introduced under the 2020 tax reform is applicable for the fiscal years beginning on or after 1 April 2022 based on a fundamental revision from the Consolidated Tax Return Filing System including the revision of the tax book value adjustment method.

Under the tax book value adjustment, which is applied immediately before the withdrawal of a subsidiary from the aggregation group, it is necessary for each company in the aggregation group holding shares in the withdrawing subsidiary to make an adjustment of the tax book value of the shares in the withdrawing subsidiary to the amount equivalent to the tax book value of the net assets of the withdrawing subsidiary.

The above tax book value adjustment will lead to the following case, for example:

- A parent company of the aggregation group acquired 100 percent of the shares in a company outside the aggregation group for an amount more than the amount equivalent to the tax book value of net assets including the positive goodwill value of the company and the acquired company participated in the aggregation group.
- Subsequently the parent company transfers the shares in the acquired company and is required to make the tax book value adjustment.
- A concern has been raised that the amount equivalent to the goodwill value is not part of the cost of the transferred shares and is not deductible from taxable income of the parent company.

In order to deal with the above concern, by virtue of the 2022 tax reform, it is proposed that the 'amount corresponding to the asset adjustment account, etc.' can be added to the amount equivalent to the tax book value of the net assets of the withdrawing subsidiary under the tax book value adjustment as far as each company in the aggregation group holding shares in the withdrawing subsidiary satisfies both of the following conditions:

[Conditions]

(i)	A detailed statement of the calculation for the 'amount corresponding to the asset adjustment account, etc.' related to the shares in the withdrawing subsidiary is attached to a final tax return, etc. for the fiscal year including the time of the withdrawal.
(ii)	Documents stating the matters which are the basis of the calculation in (i) above are preserved.

[Considerations]

- The above amendments will also be applied to the subsidiaries shifted to the JGR from the Consolidated Tax Return Filing System.

- The above measures will not be applied to the subsidiaries in the aggregation group which are subject to the crystallization of built-in gains/losses due to the case that main business of the subsidiary will not be expected to be continued.

[Definition of key terms]

Amount corresponding to the asset adjustment account, etc.	Among the acquisition costs of the shares in the subsidiary (withdrawing subsidiary) acquired at market value by the companies in the aggregation group before the withdrawing subsidiary started or participated in the JGR, the amount equivalent to the amount calculated as the asset adjustment account or the liability adjustment account based on the assumption that the acquisition costs are deemed to be the consideration for the non-tax qualified merger, in which the withdrawing subsidiary is assumed as a merged company.	
	<ul style="list-style-type: none"> Where the shares in the withdrawing subsidiary are gradually acquired at market value Where the shares in the withdrawing subsidiary are acquired at market value by multiple companies in the aggregation group 	Total amount of the following: [The amount corresponding to the amount calculated as the adjustment account at the time of each acquisition by each company] x [Acquisition ratio of the shares]
	<ul style="list-style-type: none"> Where a non-qualified tax merger, etc. is conducted in which the withdrawing subsidiary is a merged company, etc. 	Zero

(2) Amendments to foreign tax credits

In order to reduce the administrative burden on taxpayers and the tax authorities, the following measures are applied to a company in the aggregation group of the JGR in principle under the 2020 tax reform, where the amount of foreign tax credits previously applied was incorrect:

Measures to fix the amount of foreign tax credits stated in the tax returns filed by the filing due date	The amount of foreign tax credits for a past fiscal year is fixed at the amount stated in the tax returns filed by the filing due date. Therefore, it is not necessary to file an amended tax return or make a correction by the tax authority for the past fiscal year.
Measures for adjustment in the current fiscal year	Any shortfall or excess between the amount of foreign tax credits stated in the tax returns and the correct amount of foreign tax credits after recalculation (amount equivalent to the shortfall of tax credits/amount equivalent to the excess of tax credits) is adjusted by deducting from or adding to the amount of corporation tax in the current fiscal year ^(*) .

(*) The amount equivalent to the shortfall of tax credits/amount equivalent to the excess of tax credits is also fixed at the amount stated in the tax returns for the fiscal year in which the measure is applied. (Hereinafter, this treatment is referred to as 'measures to fix the amount equivalent to the shortfall of tax credits, etc.')

By virtue of the 2022 tax reform, the above measures will be amended as follows and other necessary measures will also be provided:

(i)	Where the 'measures for adjustment in the current fiscal year' should be applied as a result of a tax audit	The tax authority explains the content of results of the tax audit (including the amount to be subject to the 'measures for adjustment in the current fiscal year' and the reason) to the audited company in the aggregation group.
(ii)	Where the amount equivalent to the shortfall of tax credits/amount equivalent to the excess of tax credits, etc. stated in the attachment of the tax returns filed by the filing due date for the fiscal year including the day on which an explanation of (i) was made, is different from the content of the explanation	The 'measures to fix the amount equivalent to the shortfall of tax credits, etc.' for the fiscal year are not applicable. (i.e. the tax authority can make a correction.)
(iii)	Where an amended tax return is filed or a correction by the tax authority is made for the amount of foreign tax credits or the amount equivalent to the shortfall of tax credits/amount equivalent to the excess of tax credits for the fiscal year in which the decision on non-application of the measures to fix the amount of tax credits, etc. is made	In principle, the measures to fix the amount of tax credits, etc. are reapplied based on the amount stated in the amended tax return or the correction notice as the amount of tax credits, etc.

Measures related to the above amendments will also be provided for local tax purposes.

(3) Other amendments

- Under the crystallization of built-in gains/losses at the time of withdrawal from the aggregation group, etc., assets with a tax book value of less than JPY10 million are not subject to the crystallization of built-in gains/losses. By virtue of the 2022 tax reform, goodwill with a tax book value of less than JPY10 million will be subject to the crystallization of built-in gains/losses.
- Where an amount equivalent to the interest tax is transferred between two companies in the aggregation group, the amount will be excluded from the tax-effect equivalent amount (the amount equivalent to the reduction in corporation tax and local corporation tax as a result of application of the JGR), which is treated as non-taxable income and non-deductible expenses.
- A certain company which does not fall under certain conditions is subject to the write-off of tax NOLs and the restriction on usage of tax NOLs and unrealized losses on certain assets. For example, one of the conditions for a parent company is the requirement for five-year continuation of a controlling relationship with any of the subsidiaries in the aggregation group. Under this rule, the requirement for a parent company, which is established five years before the approval date of the JGR, will be amended. (Special provision for the requirement for five-year continuation of a controlling relationship for the subsidiaries in the aggregation group will also be amended.)
- In connection with the special measures of tax NOLs applied to companies conducting certain certified business by the Japanese

government, the allocation method of deductible limit of non-specific tax NOLs to each company in the aggregation group will be amended.

- Other necessary measures will also be provided.

Although the timing of application of the above amendments is not specified in the Proposal, it is expected that the above amendments will be applicable from the fiscal years beginning on or after 1 April 2022 in line with the timing of the application of the JGR.

II. International Taxation

1. Special Provision for Reduction of Book Value of Shares in Subsidiaries

By virtue of the 2020 tax reform, the Special Provision for Reduction of Book Value of Shares in Subsidiaries was introduced to prevent tax avoidance by creation of a capital loss from the transfer of shares in a subsidiary after receiving dividends from such subsidiary. Under the special provision, in order to prevent such creation of a capital loss, where a Japanese company receives certain dividends ('Covered Dividends') from certain subsidiaries, the tax book value of shares in the subsidiary is reduced by the amount equivalent to the portion of dividends treated as non-inclusion income and the same amount is also deducted from the balance of tax earnings and profits of the Japanese company.

By virtue of the 2022 tax reform, the exemption rule and the rules for preventing tax evasion by using the exemption rule will be amended as follows and other necessary measures will also be provided:

(1) Amendments to exemption rule (requirement of retained earnings at the specified control date)

The special provision does not apply to the cases where any of (i) requirement of domestic shareholders ratio (90% threshold), (ii) requirement of retained earnings at the specified control date, (iii) requirement of specified control period (10 years threshold) or (iv) amount of dividends (JPY20 million threshold) is satisfied.

The requirement of (ii) is to exclude the 'Covered Dividends' from the scope of the special provision given the conditions that relevant documents are preserved, where the amount of retained earnings of a subsidiary at the end of the 'Preceding Fiscal Year' after the deduction of the amount of dividends received by shareholders of a subsidiary for the period from the day following the end of the 'Preceding Fiscal Year' up to the time of receipt of the 'Covered Dividends' is not less than the amount of retained earnings of a subsidiary at the end of the latest fiscal year ending before the 'Specified Control Date'. This is because such payment can be deemed as the payment out of the profits generated after the Japanese company acquired the subsidiary.

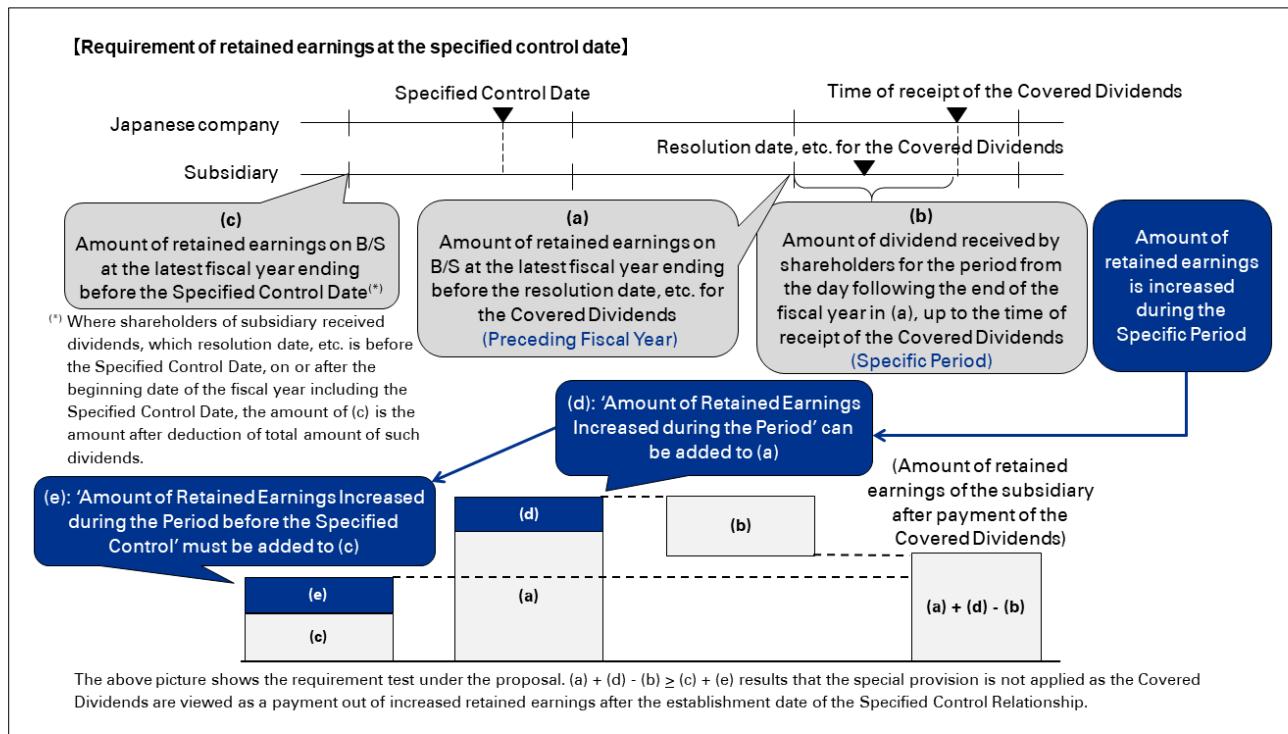
The requirement (ii) under the current tax law does not cover the case where the 'Covered Dividends' are paid out of the amount that retained

earnings have increased by during the fiscal year including the payment date of such 'Covered Dividends'. As a result, there may be cases where the requirement (ii) cannot be satisfied. By virtue of the 2022 tax reform, the following amendments to the requirement (ii) will be provided to cover such cases:

Conditions	Where the amount of retained earnings of a subsidiary is increased during the 'Specific Period', and any of the resolution date, etc. for the dividends received by shareholders from the subsidiary during the 'Specific Period' is on or after the day following the end of the 'Preceding Fiscal Year' (Given the conditions that certain documents, which prove the 'Amount of Retained Earnings Increased during the Period' and 'Amount of Retained Earnings Increased during the Period before the Specified Control', are preserved)
Adjustment of retained earnings	The 'Amount of Retained Earnings Increased during the Period' can be added to the amount of retained earnings on the balance sheet of the subsidiary for the 'Preceding Fiscal Year'. (Where the adjustment is applied, the 'Amount of Retained Earnings Increased during the Period before the Specified Control' must also be added to the amount of retained earnings on the balance sheet of the subsidiary at the end of the latest fiscal year ending before the 'Specified Control Date'.)

[Definition of key terms]

Covered Dividends	The amount of dividends received by a Japanese company from a subsidiary with a 'Specified Control Relationship', excluding deemed dividends from the subsidiary with a 100% control relationship
Specified Control Relationship	Control relationship between the parties or the relationship between companies where both are controlled by the same person/company
Specified Control Date	The date on which a Japanese company most recently came to have a 'Specified Control Relationship' with a subsidiary
Preceding Fiscal Year	Latest fiscal year of a subsidiary ending before the resolution date, etc. for the 'Covered Dividends'
Specific Period	Period from the day following the end of the 'Preceding Fiscal Year' up to the time of receipt of the 'Covered Dividends'
Amount of Retained Earnings Increased during the Period	Total amount of the following: <ul style="list-style-type: none"> The amount retained earnings of a subsidiary increased during the 'Specific Period' The amount retained earnings of a subsidiary decreased corresponding to the amount of dividends received by shareholders of a subsidiary during the 'Specific Period'
Amount of Retained Earnings Increased during the Period before the Specified Control	Total amount of the following, if the amount of retained earnings of a subsidiary was increased during the 'Specific Period before the Specified Control', and shareholders received the dividends (limited to where the resolution date, etc. for the dividends is within the 'Specific Period before the Specified Control') from a subsidiary: <ul style="list-style-type: none"> The amount retained earnings of a subsidiary increased during the 'Specific Period before the Specified Control' The amount retained earnings of a subsidiary decreased corresponding to the amount of dividends received by shareholders of a subsidiary during the 'Specific Period before the Specified Control'
Specific Period before the Specified Control	Period from the beginning date of the fiscal year including the 'Specified Control Date' up to the day prior to the 'Specified Control Date'



(2) Amendments to rules for preventing tax evasion by using exemption rule

Rules for preventing tax evasion are provided under the special provision in order to prevent an inappropriate application of the exemption rule by manipulation among the group companies.

By virtue of the 2022 tax reform, one of the rules, which is applied to the case using dividend payments through subsidiaries satisfying the conditions for the exemption rule, will be amended in order not to apply this rule in either of the following cases:

(i)	Where all of the 'Second-Tier Subsidiaries, etc.' are 'Continuously Related Companies' (Excluding the case where a subsidiary or 'Second-Tier Subsidiary, etc.' was the surviving company after a merger with a company that was not a 'Continuously Related Company', etc.)
(ii)	Where both of the following conditions are satisfied: <ul style="list-style-type: none"> (a) Where a second-tier subsidiary have a 'Specified Control Relationship' with the parent company continuously from the date of establishment of the second-tier subsidiary to the resolution date, etc. for the dividends received by the subsidiary from the second-tier subsidiary (b) Where all of the 'Third-Tier Subsidiaries, etc.' are 'Continuously Related Companies' (Excluding the case where a second-tier subsidiary or 'Third-Tier Subsidiary, etc.' was the surviving company after a merger with a company that was not a 'Continuously Related Company', etc.)

[Definition of key terms]

Second-Tier Subsidiary, etc.	A company which had a 'Specified Control Relationship' with a subsidiary within 10 years prior to the resolution date, etc. for the 'Covered Dividends'	
Third-Tier Subsidiary, etc.	A company which had a 'Specified Control Relationship' with a second-tier subsidiary within 10 years prior to the resolution date, etc. for the dividends received by a subsidiary from the second-tier subsidiary	
Continuously Related Company	In case of (i)	A company (lower tier company of a subsidiary) which has a 'Specified Control Relationship' with the subsidiary continuously from the date of establishment of the company to the resolution date, etc. for the 'Covered Dividends' (in the case of a 'Second-Tier Subsidiaries, etc.' which did not have the 'Specified Control Relationship' prior to the resolution date, etc., the time immediately prior to the latest date on which the 'Second-Tier Subsidiaries, etc.' came not to have the 'Specified Control Relationship')
	In case of (ii)(b)	A company (lower tier company of a second-tier subsidiary) which has a 'Specified Control Relationship' with the second-tier subsidiary continuously from the date of establishment of the company to the resolution date, etc. for the dividends received by a subsidiary from the second-tier subsidiary (in the case of a 'Third-Tier Subsidiaries, etc.' which did not have the 'Specified Control Relationship' prior to the resolution date, etc., the time immediately prior to the latest date on which the 'Third-Tier Subsidiaries, etc.' came not to have the 'Specified Control Relationship')

(3) Timing of application

The amendments of (1) and (2) above will be applied to the 'Covered Dividends' received in the fiscal years beginning on or after 1 April 2020.

2. Earnings Stripping Rules

Under the earnings stripping rules (ESRs), the deduction of net interest payments in excess of 20 percent of adjusted taxable income is disallowed in order to prevent tax avoidance by the payment of excess interest compared to the size of taxable income. For foreign companies, the ESRs are applied to Japanese source income attributable to their permanent establishments (PE).

By virtue of the 2022 tax reform, the scope of application to foreign companies will be amended. Specifically, the ESRs will also be applied to the amount of income relating to the following Japanese source income that is subject to corporation tax for foreign companies:

- Japanese source income not attributable to a PE of a foreign company having a PE in Japan
- Japanese source income of a foreign company not having a PE in Japan

III. Improvements in Tax Administration Matters

1. Electronic Preservation System for Account Books, etc.

(1) Development of scanner preservation system for national tax-related documents, etc. corresponding to the establishment of the certification system of the time stamp by the Japanese government

The scanner preservation system for national tax-related documents and preservation system for electromagnetic records related to transaction information of electronic transactions require a preservation obligor to put a time stamp certified by the Japan Data Communications Association on the recorded matters in electromagnetic records of the national tax-related documents or transaction information of electronic transactions within a certain period.

By virtue of the 2022 tax reform, corresponding to the establishment of the certification system of the time stamp by the Japanese government, the above time stamp will be replaced by the time stamp certified by the Minister of Internal Affairs and Communications for the electromagnetic records of the national tax-related documents or transaction information of electronic transactions that are preserved on or after 1 April 2022.

A transitional measure will be provided that the current time stamp certified by the Japan Data Communications Association is also applicable for the period from 1 April 2022 to 29 July 2023.

Local tax will be also amended in line with the above amendments.

(2) Transitional measures for smooth transition to preservation system for electromagnetic records related to transaction information of electronic transactions

The current law allows the preservation of output documents, etc. of the electromagnetic records related to transaction information of electronic transactions (e.g. electromagnetic records of invoices, etc. sent and received by e-mail, etc.) instead of the electromagnetic records.

The 2021 tax reform repealed the above treatments for output documents, etc. and requires a preservation obligor to preserve the electromagnetic records under certain conditions (i.e. ensuring search functionality, etc.) on or after 1 January 2022. Therefore, the preservation obligors, who currently preserve output documents, etc. of the electromagnetic records related to transaction information of electronic transactions, have been proposing establishment of the transitional measures by which preservation obligors can have sufficient time for the preparation of system development to comply with the 2021 tax reform and remove concern on the cancellation of approval for blue return filing due to non-compliance with the requirements under the 2021 tax reform.

By virtue of the 2022 tax reform, transitional measures will be provided that allow the preservation of the electromagnetic records related to transaction information of electronic transactions for the period from 1

January 2022 to 31 December 2023 conducted by a preservation obligor of individual income tax (except for withholding income tax) and corporation tax regardless of the preservation requirements under the 2021 tax reform, as far as the following (i) and (ii) are satisfied:

(i)	The competent tax office acknowledges unavoidable reasons for the failure of the preservation of the electromagnetic records related to transaction information of electronic transactions in compliance with the preservation requirements under the 2021 tax reform.
(ii)	The preservation obligor follows the request for presentation or submission of output documents of the electromagnetic records related to transaction information of electronic transactions (limited to output documents in an orderly form and in a clear state) by the National Tax Agency, etc. based on its right of question and inspection.

The above amendments will be applied for transaction information of electronic transactions conducted on or after 1 January 2022.

Where the above measures are applied, the tax authority will pay attention to the actual situation of a preservation obligor who has difficulty to comply with the preservation requirements of the electromagnetic records under the 2021 tax reform, and will give the preservation obligor appropriate consideration by which the preservation obligor is allowed to preserve the output documents, etc. without any procedures to the competent tax office.

2. Reporting Requirement for Assets/Liabilities and Overseas Assets

(1) Amendments to 'Statement of Assets/Liabilities'

From the viewpoint of reducing the administrative burden on individuals obliged to submit the 'Statement of Assets/Liabilities' and ensuring appropriate taxation, the reporting requirement for assets/liabilities will be amended as follows:

	Current tax law	Proposal
Person obliged to submit statements	<ul style="list-style-type: none"> An individual who has a filing obligation of their income tax return and meets the following two criteria: <ul style="list-style-type: none"> (i) Total income exceeds JPY20 million for a calendar year (ii) Total value of assets as of the end of a calendar year is JPY300 million or more <ul style="list-style-type: none"> or Total value of financial assets (e.g. securities) as of the end of a calendar year is JPY100 million or more 	<p>An individual who meets the following criteria <u>in addition to</u> individuals who are currently subject to reporting obligation:</p> <ul style="list-style-type: none"> <u>A resident whose assets have a total value of JPY1 billion or more as of the end of a calendar year (No criteria based on the size of income)</u>
Due date for submission	15 March of the following year	<u>30 June</u> of the following year

Scope of omissible items	'Household movables that fall under the category of other movables' whose acquisition cost is less than JPY1 million	'Household movables that fall under the category of other movables' whose acquisition cost is less than <u>JPY3 million</u>
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Other than the above, operational amendments to items to be declared in the 'Statement of Assets/Liabilities' will be proposed.

These amendments will apply to the 'Statement of Assets/Liabilities' for 2023 and thereafter.

Under the current tax law, when a 'Statement of Assets/Liabilities' is submitted after the due date for submission, the 'Statement of Assets/Liabilities' is deemed to have been submitted within the deadline unless it was submitted in anticipation of correction or determination due to a tax audit. By virtue of the 2022 tax reform, this measure will apply only in cases where the submission was made before a notification of a tax audit. This amendment will be applicable to the 'Statement of Assets/Liabilities' submitted on or after 1 January 2024.

(2) Amendments to 'Statement of Overseas Assets'

From the viewpoint of reducing the administrative burden on individuals obliged to submit the 'Statement of Overseas Assets', the reporting requirement for overseas assets will be amended as follows:

	Current tax law	Proposal
Due date for submission	15 March of the following year	<u>30 June</u> of the following year

Other than the above, operational amendments to items to be declared in the 'Statement of Overseas Assets' will be proposed.

These amendments will apply to the 'Statement of Overseas Assets' for 2023 and thereafter.

Under the current tax law, when a 'Statement of Overseas Assets' is submitted after the due date for submission, the 'Statement of Overseas Assets' is deemed to have been submitted within the deadline unless it was submitted in anticipation of correction or determination due to a tax audit. By virtue of the 2022 tax reform, this measure will apply only in cases where the submission was made before a notification of a tax audit. This amendment will be applicable to the 'Statement of Overseas Assets' submitted on or after 1 January 2024.

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