

KPMG Japan Tax Newsletter

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OUTLINE OF THE 2023 TAX REFORM PROPOSALS

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The ruling coalition (the Liberal Democratic Party and Komeito) agreed on the 'Outline of the 2023 Tax Reform Proposals' ('Proposal') on 16 December 2023. 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 R&D Costs

(1) Tax credits for general R&D costs

By virtue of the 2023 tax reform, in order to further strengthen incentives to increase investment in R&D, the rules concerning the tax credits for general R&D costs (under which the creditable amount is calculated by multiplying total R&D costs by the creditable ratio discussed below) will be amended as follows:

(i) Large-sized companies

[Current tax law]

■ Basic rule

Increase-decrease R&D ratio	Creditable ratio ^(*)
More than 9.4% ^(**)	10.145% + (Increase-decrease R&D ratio - 9.4%) x 0.35 (Upper limit: 14%)
9.4% or less	10.145% - (9.4% - Increase-decrease R&D ratio) x 0.175 (Lower limit: 2%) ^(***)

^(*) 8.5 percent is applied for a fiscal year including the date of establishment or a fiscal year when the annual average of R&D costs for the preceding 3 fiscal years is zero.

^(**) Not applicable for fiscal years beginning on or after 1 April 2023

^(***) Upper limit will be 10 percent for fiscal years beginning on or after 1 April 2023.

Maximum tax credit	
Companies other than below	Corporation tax liability x 25%
Companies increasing investment in R&D in spite of a certain degree of decrease in sales ^(*)	Corporation tax liability x 30%
Certain venture R&D companies	Corporation tax liability x 40%

^(*) Applicable for fiscal years satisfying both of the following conditions for each fiscal year beginning between 1 April 2021 and 31 March 2023:

- Ratio of decrease in sales compared to that in the base year ≥ 2 percent
- R&D costs > R&D costs in the base year

■ Temporary measures where R&D ratio exceeds 10 percent

Both of the following measures are available for fiscal years beginning between 1 April 2019 and 31 March 2023:

Creditable ratio (Upper limit: 14%)	Creditable ratio (under the basic rule)	+	Creditable ratio (under basic rule) $\times \{(R\&D \text{ ratio} - 10\%) \times 0.5 \text{ (Upper limit: 10\%)}\}$
Maximum tax credit	Maximum tax credit (under the basic rule)	+	Corporation tax liability $\times \{(R\&D \text{ ratio} - 10\%) \times 2\}$ (Upper limit: corporation tax liability $\times 10\%$)

[Proposal]

■ Basic rule

The following underlined items will be amended:

Increase-decrease R&D ratio	Creditable ratio ^(*)
More than <u>12%</u> ^{(*)2}	<u>11.5%</u> + (Increase-decrease R&D ratio - <u>12%</u>) \times <u>0.375</u> (Upper limit: 14%)
<u>12%</u> or less	<u>11.5%</u> - (<u>12%</u> - Increase-decrease R&D ratio) \times <u>0.25</u> (Lower limit: <u>1%</u>) ^{(*)3}

(*) 8.5 percent is applied for a fiscal year including the date of establishment or a fiscal year when the annual average of R&D costs for the preceding 3 fiscal years is zero.

(*)2 Not applicable for fiscal years beginning on or after 1 April 2026

(*)3 Upper limit will be 10 percent for fiscal years beginning on or after 1 April 2026.

Maximum tax credit ^(*)	
Companies other than below	Corporation tax liability \times 25%
Certain venture R&D companies	Corporation tax liability \times 40%

(*) Temporary measures regarding maximum tax credit for 'Companies increasing investment in R&D in spite of a certain degree of decrease in sales' (please refer to [Current tax law]) will be abolished at the end of the applicable period.

■ Temporary measures where R&D ratio exceeds 10 percent

The applicable period will be extended by 3 years (fiscal years beginning on or before 31 March 2026). (There is no change in the contents of temporary measures.)

■ Temporary measure for maximum tax credit corresponding to the Increase-decrease R&D ratio

The following temporary measure for the maximum tax credit will be introduced for fiscal years beginning between 1 April 2023 and 31 March 2026:

Increase-decrease R&D ratio	Maximum tax credit ^(*)
More than 4%	'Corporation tax liability x 0.625%' is added per 1%. (Upper limit: 5%)
Below minus 4%	'Corporation tax liability x 0.625%' is subtracted per 1%. (Upper limit: 5%)

^(*) Where R&D ratio exceeds 10 percent, the larger maximum tax credit of this temporary measure or the 'Temporary measures where R&D ratio exceeds 10 percent' will be applied.

(ii) Small and medium-sized companies

[Current tax law]

■ Basic rule

Increase-decrease R&D ratio	Creditable ratio
More than 9.4% ^(*)	12% + (Increase-decrease R&D ratio - 9.4%) x 0.35 (Upper limit: 17%)
9.4% or less	12%

^(*) Applicable for fiscal years beginning between 1 April 2021 and 31 March 2023 excluding a fiscal year including the date of establishment or a fiscal year when the annual average of R&D costs for the preceding 3 fiscal years is zero

Increase-decrease R&D ratio	Maximum tax credit	
	More than 9.4% ^(*) ^(*)	Principle
Companies increasing investment in R&D in spite of a certain degree of decrease in sales ^(*)		Corporation tax liability x 40%
9.4% or less	Principle	Corporation tax liability x 25%
	Companies increasing investment in R&D in spite of a certain degree of decrease in sales ^(*)	Corporation tax liability x 30%

^(*) Applicable for fiscal years beginning between 1 April 2021 and 31 March 2023 excluding a fiscal year including the date of establishment or a fiscal year when the annual average of R&D costs for the preceding 3 fiscal years is zero

^(*) The 'maximum tax credit' under the 'Temporary measures where R&D ratio exceeds 10 percent' is not applicable.

(^{*3}) Applicable for fiscal years satisfying the same conditions as for large-sized companies

■ Temporary measures where R&D ratio exceeds 10 percent

Both of the following measures are available for fiscal years beginning between 1 April 2019 and 31 March 2023:

Creditable ratio (Upper limit: 17%)	Creditable ratio (under the basic rule)	+	Creditable ratio (under the basic rule) x {(R&D ratio - 10%) x 0.5 (Upper limit: 10%)}
Maximum tax credit	Maximum tax credit (under the basic rule)	+	Corporation tax liability x {(R&D ratio - 10%) x 2} (Upper limit: corporation tax liability x 10%)

[Proposal]

■ Basic rule

The following underlined items will be amended:

Increase-decrease R&D ratio	Creditable ratio
More than <u>12%</u> ^(*)	12% + (Increase-decrease R&D ratio - <u>12%</u>) x <u>0.375</u> (Upper limit: 17%)
<u>12%</u> or less	12%

(^{*}) Applicable for fiscal years beginning between 1 April 2023 and 31 March 2026 excluding a fiscal year including the date of establishment and a fiscal year when the annual average of R&D costs for the preceding 3 fiscal years is zero

Increase-decrease R&D ratio	Maximum tax credit ^(^{*3})
More than <u>12%</u> ^{(^{*1})(^{*2})}	Corporation tax liability x 35%
<u>12%</u> or less	Corporation tax liability x 25%

(^{*1}) Applicable for fiscal years beginning between 1 April 2023 and 31 March 2026 excluding a fiscal year including the date of establishment or a fiscal year when the annual average of R&D costs for the preceding 3 fiscal years is zero

(^{*2}) The 'maximum tax credit' under the 'Temporary measures where R&D ratio exceeds 10 percent' is not applicable.

(^{*3}) Temporary measures regarding maximum tax credit for 'Companies increasing investment in R&D in spite of a certain degree of decrease in sales' (please refer to [current tax law]) will be abolished at the end of the applicable period.

■ Temporary measures where R&D ratio exceeds 10 percent

The applicable period will be extended by 3 years (fiscal years beginning on or before 31 March 2026). (There is no change in the contents of temporary measures.)

[Definition of key terms]

- Large-sized companies: Companies other than small and medium-sized companies
- Small and medium-sized companies: (a) or (b) below:
 - (a) 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
 - (b) Companies with no capital whose number of regular employees is 1,000 or less

Note that a company whose average income for the preceding 3 fiscal years is over JPY1.5 billion is excluded from the definition of small and medium-sized companies for the purpose of this measure.

- Increase-decrease R&D ratio: (a) / (b)
 - (a) [Total R&D costs in the current fiscal year] – [Annual average of R&D costs for the preceding 3 fiscal years] (if the figure is negative, the negative figure is used.)
 - (b) Annual average of R&D costs for the preceding 3 fiscal years
- Certain venture R&D companies: Companies which were established within the past 10 years and have tax losses to be carried forward (Subsidiaries of a large company are not eligible.)
- Ratio of decrease in sales compared to those in the base year: ((b) – (a)) / (b), where (a) is less than (b)
 - (a) Sales in the current fiscal year
 - (b) Sales in the latest fiscal year ending before 1 February 2020
- R&D costs in the base year: R&D costs in the latest fiscal year ending before 1 February 2020
- R&D ratio: Total R&D costs in the current fiscal year / Average sales
- Average sales: Average sales for the preceding 3 fiscal years and the current fiscal year

(2) Tax credits for specified R&D costs

Specified R&D costs are eligible for the special rules under which the creditable amount is calculated by multiplying specified R&D costs by the creditable ratio discussed below.

By virtue of the 2023 tax reform, from the viewpoint of improving the quality of R&D, scope of specified R&D costs will be expanded. In order to promote open innovation between existing companies and start-ups, and investment in R&D personnel, joint/consignment R&D with/to R&D venture companies will be excluded from the scope, and the underlined items will be newly treated as specified R&D costs.

Scope of specified R&D costs (R&D costs used for the following R&D activities)		Creditable ratio
Joint R&D with	National R&D institutions	30%
	Universities	
	<u>Special Companies Developing New Business</u>	<u>25%</u>
	Externalized companies of national R&D companies, etc.	
	Private enterprises	20%
	R&D partnerships	
Consignment R&D to	National R&D institutions	30%
	Universities	
	<u>Special Companies Developing New Business</u>	<u>25%</u>
	Externalized companies of national R&D companies, etc.	
	Specified small and medium-sized companies	20%
	Certain private enterprises	
Royalties on intellectual property	Specified small and medium-sized companies	20%
R&D concerning orphan drug or medicine products with special use		20%
<u>Labor costs for certain postdoctoral employees, etc. involved in R&D activities among R&D costs^(*)</u>		<u>20%</u>

(*) Limited to those satisfying certain requirements

(3) Scope of R&D costs under the tax credit system

(i) Inclusion in the scope of R&D costs

Under the current tax law, R&D costs for development of new services using existing big data are excluded from the scope of R&D costs since one of the requirements to be treated as 'R&D Costs related to development of new services provided for consideration' is collection of new big data.

By virtue of the 2023 tax reform, in order to develop new business models, R&D costs for development of new services using existing big data will be included in the scope of R&D costs under the tax credit system.

(ii) Exclusion from the scope of R&D costs

By virtue of the 2023 tax reform, costs for designs and prototypes based on devised designs as part of development work, which are obviously not intended to improve performance, will be excluded from the scope of R&D costs under the tax credit system.

In addition, necessary measures will be provided.

2. Special Measures for Promoting Open Innovation

Where blue-return filing companies, who conduct specified business activities,^(*) acquire shares of a start-up ('Special Companies Developing New Business') that meet certain conditions ('Specified Shares') during the period from 1 April 2020 to 31 March 2024, the amount equivalent to 25 percent of the acquisition cost of the Specified Shares is allowed to be included in deductible expenses in the fiscal year including the day of acquisition.

^(*) Specified business activities mean business activities aimed towards undertaking business by which high productivity or developing new business are expected by utilizing management resources other than the company's own management resources.

By virtue of the 2023 tax reform, the following amendments are proposed in order to promote strongly the growth of start-ups:

(1) Requirements for Specified Shares

Under the current tax law, Specified Shares need to be issued by a cash contribution for capital increase of the Special Companies Developing New Business. Therefore, the special measures are not applied to the acquisition of shares by purchasing issued shares.

By virtue of the 2023 tax reform, shares acquired by purchasing issued shares will also be included in the scope of the Specified Shares in order to apply the special measures to M&As of start-ups and the requirements for Specified Shares will be amended as follows:

	Requirements for Specified Shares		
	Acquisition method of Specified Shares	Requirements for acquisition cost per case	Requirement for estimated holding period
Current tax law	Cash contribution for capital increase	<ul style="list-style-type: none"> • Payment by large-sized companies^(*1): JPY100 million or more • Payment by small and medium-sized companies^(*1): JPY10 million or more • Payment to foreign companies: uniformly JPY500 million or more 	Over 3 years
Proposal	Cash contribution for capital increase ^(*2)	<ul style="list-style-type: none"> • Payment by large-sized companies: JPY100 million or more • Payment by small and medium-sized companies: JPY10 million or more • Payment to foreign companies: uniformly JPY500 million or more 	Over 3 years
	Purchase from a person other than the issuing company (Limited to the cases where the resulting shareholding ratio is more than 50% of the total voting rights) ^{(*3) (*4)}	JPY500 million or more	Over 5 years

^(*1) Please refer to [Definition of key terms] in '1. Tax Credits for R&D Costs.'

^(*2) Investments in Special Companies Developing New Business made by the shareholder, who already holds more than 50 percent of the total voting rights, will be excluded from the application of the special measures. In addition, the application of the special measures for investments in Special Companies Developing New Business made by the shareholder, who holds 50 percent or less of the total voting rights using the special measures, will be limited to the cases where the resulting shareholding ratio is more than 50 percent of the total voting rights by the investments.

^(*3) Limited to shares of domestic companies

^(*4) Shares of Special Companies Developing New Business, which are acquired after the application of the special measures by cash contribution for capital increase to the Special Companies Developing New Business on or after 1 April 2023, will not be eligible for the special measures.

(2) Upper limit of the acquisition cost of Specified Shares subject to the special measures

Under the special measures, when Specified Shares are acquired, given the conditions that the special account is recorded in the account books for the amount equivalent to 25 percent or less of the acquisition cost (up to the upper limit) of the Specified Shares in the fiscal year including the day of the acquisition, the amount accounted for the special account is allowed to be included in deductible expenses.

By virtue of the 2023 tax reform, the upper limit of the acquisition cost of Specified Shares under the special measures will be amended as follows:

Acquisition method of Specified Shares	Current tax law	Proposal
Cash contribution for capital increase	JPY10 billion	JPY5 billion
Purchase from a person other than the issuing company	/	JPY20 billion

(3) Cause for reversal of special account

Where the cause for reversal of the special account occurs, the reversed amount, which had been deducted in the fiscal year including the day of the acquisition, shall be included in taxable income in the fiscal year including the day on which the cause for reversal occurred (except for the case that the Minister of Economy, Trade and Industry has certified that the period of 3 years or more has elapsed since the acquisition of the Specified Shares).

In order to promote M&As that truly contribute to the growth of start-ups, the causes for reversal of the special account related to Specified Shares acquired by purchasing from a person other than the issuing company, which will be added by the 2023 tax reform, will be provided as follows after the amendments of the current causes for reversal:

(The causes for reversal will be the same as the current causes for reversal except for the following.)

	Causes for reversal	Amount of reversal
(i)	Where 5 years have elapsed since the acquisition of the Specified Shares (Note that the cases will be excluded where the requirements such as that the sales amount in any fiscal year becomes 1.7 times or more and JPY3.3 billion or more within 5 years from the day of acquisition are satisfied.)	The amount in the special account
(ii)	Where the Special Company Developing New Business issuing the Specified Shares was dissolved as a result of a merger in case that the company recording the special account is a surviving company	The amount in the special account

(iii)	Where the company recording the special account ceases to hold more than 50% of the total voting rights of the Special Companies Developing New Business issuing the Specified Shares	The amount in the special account
(iv)	In the case described in parentheses in (i) above, where any of the current causes for reversal (excluding the causes that the continuous certification of special business activities was not provided and the investment ratio in an Investment Limited Partnership, etc. holding the Specified Shares in its assets was changed) occurs after 5 years have elapsed since the acquisition of the Specified Shares	The amount in the special account according to the cause for reversal
(v)	In the case described in parentheses in (i) above, where the investment ratio in an Investment Limited Partnership, etc. holding the Specified Shares in its assets was reduced	The amount in the special account corresponding to the ratio of decrease
(vi)	In the case described in parentheses in (i) above, where the company recording the special account received dividends on the Specified Shares	The amount equivalent to 25% of the amount of received dividends

In addition to the above, necessary measures will be provided.

3. Special Measures for Promoting Investment in Digital Transformation

From the viewpoint of promoting business process re-engineering through digital technology, blue-return filing companies satisfying certain requirements are allowed to apply a tax credit (3% or 5%) or special depreciation (30%) on the acquisition cost of software and the amount of related deferred charges, where the companies make such investments during the period from 2 August 2021 to 31 March 2023 in accordance with plans for business adaptation certified by the competent minister under the Industrial Competitiveness Enhancement Act.

By virtue of the 2023 tax reform, the following are proposed:

- The conditions for improvement of productivity or development of new demand for goods and services will be amended.
- The applicable period of the special measures will be extended by 2 years to 31 March 2025.

Please note that this measure will not be applied to assets acquired on or after 1 April 2023 in accordance with plans for business adaptation where certification was applied for before 1 April 2023.

Necessary measures will be provided for individual income tax purposes in line with the above amendments.

4. Spin-Off Transactions

Under the current tax law, certain types of spin-off transactions (e.g. Share-dividends (Kabushiki-bunpai) in which a company distributes all of the shares in its wholly owned subsidiary to its shareholders) are treated as tax-qualified reorganizations provided that certain conditions are met.

By virtue of the 2023 tax reform, the following partial spin-off to be treated as a tax-qualified reorganization will be introduced as a temporary measure so that a company can retain a certain portion of the shares in its wholly owned subsidiary by spin-off of its business in phases:

Eligible period	From 1 April 2023 to 31 March 2024
Outline of the partial spin-off	<p>Dividends-in-kind made as a specified dividend of surplus under the Industrial Competitiveness Enhancement Act ('Act') by a company, whose business restructuring plan is certified under the Act during the eligible period, will be treated as a Share-dividend, where the shares in its wholly owned subsidiary are transferred.</p> <p>The above dividends-in-kind satisfying the following conditions will be treated as a tax-qualified Share-dividend:</p>
Conditions	<ul style="list-style-type: none"> • Only shares in the wholly owned subsidiary will be distributed according to the number of shares held by the shareholders of the distributing company. • The number of shares in the wholly owned subsidiary held by the distributing company immediately after the dividends-in-kind is less than 20% of the total issued shares. • Approximately 90% or more of directors/employees of the wholly owned subsidiary are expected to continue working for the subsidiary. • No party owns more than 50% of the distributing company before the dividends-in-kind and it is expected that no party will own more than 50% of the wholly owned subsidiary after the dividends-in-kind. • It is expected that the main business of the wholly owned subsidiary will be continuously carried on by the subsidiary. • At least one of the specified directors of the wholly owned subsidiary does not resign due to the dividends-in-kind. • Certain conditions are satisfied, such as that stock options are granted or are expected to be granted to specified directors of the related company or the foreign related company related to the certified plan.

II. International Taxation

1. GloBE Rule - Income Inclusion Rule

(1) Outline of amendments

By virtue of the 2023 tax reform, the Income Inclusion Rule ('IIR'), which is one of the parts of the Global Anti-Base Erosion Rule ('GloBE Rule') of 'Pillar 2' agreed by the OECD/G20 Inclusive Framework on BEPS, will be enacted in light of the progress of international discussions on the details of the rules and trends toward its implementation in other countries, etc.

Items for which implementation details are expected to be discussed in the OECD after 2023, including Undertaxed Profits Rule ('UTPR') and Qualified Domestic Minimum Top-up Tax ('QDMTT'), will be enacted by the 2024 tax reform or after.

[\[Reference information\]](#)

The policy of the national and local governments in the introduction of 'Pillar 2' is stated in the Proposal as follows:

IIR/ UTPR	<ul style="list-style-type: none"> The IIR and UTPR are mechanisms for Japanese companies to be taxed based on the income earned by foreign companies. Since these tax bases are not related to the benefits received from the administrative services provided by local governments, corporate inhabitant tax and corporate business tax (including special business tax) will not be imposed. New tax measures will be designed based on the current tax rates so that the ratio of the corporation tax amount to the local corporation tax amount will be 907 to 93.
QDMTT	<ul style="list-style-type: none"> The QDMTT is a mechanism to levy tax based on the income earned by Japanese companies, etc. Since the tax base is considered to correspond to the benefits received from the administrative services provided by local governments, new tax measures will be designed based on the ratio of tax rates (breakdown of the effective statutory corporate income tax rate of 29.74%) of national and local corporate taxation. From the perspective of simplification of the system, the amount equivalent to the corporate inhabitant tax and corporate business tax imposed by the QDMTT will be collected by the national government as local corporation tax and distributed to the local governments by the national government using the current local tax allocation system. Considering the above, the ratio of the corporation tax amount to the local corporation tax amount will be 753 to 247.

As for 'Pillar 1', the goal is to achieve the sign-off of a multilateral convention by the first half of 2023. The Proposal states that the taxation system in Japan, etc. will be examined based on the provisions of the multilateral convention, etc. to be developed in the future, taking into account the national and local corporate taxation systems.

(2) Introduction of new tax measures for ‘corporation tax on the international minimum tax amount for each applicable fiscal year’

By virtue of the 2023 tax reform, new tax measures equivalent to the IIR, ‘corporation tax on international minimum tax amount for each applicable fiscal year’ (national tax) will be introduced.

(i) Outline of new tax measures for ‘corporation tax on international minimum tax amount for each applicable fiscal year’

The taxpayers, scope of taxation and calculation method of the tax base (‘international minimum tax amount’) under the new tax measures are as follows:

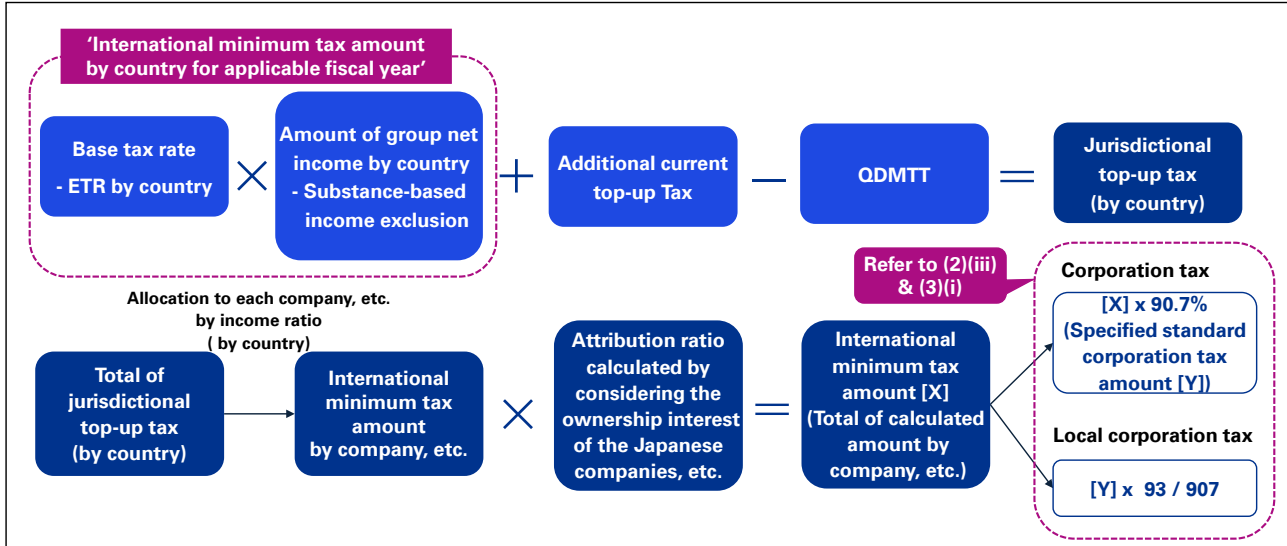
Based on the information provided in the Proposal, it seems that the new tax measures are almost the same as the IIR put forward by the OECD.

Taxpayers and scope of taxation	<ul style="list-style-type: none"> Japanese companies (excluding public interest companies) belonging to the Specified Multinational Enterprise (MNE) Groups, etc. will be subject to the ‘corporation tax on international minimum tax amount for each applicable fiscal year’^(*). The Specified MNE Group, etc. means as follows: An enterprise group, etc. (limited to those that fall under the MNE Group, etc.) that has annual revenue equivalent to EUR750 million or more in at least two of the latest four applicable fiscal years immediately preceding the tested applicable fiscal year. <p>^(*) The ‘applicable fiscal year’ is the period of the consolidated financial statements prepared by the ultimate parent companies, etc. of a Specified MNE Group, etc.</p>
Calculation method of the ‘international minimum tax amount’	<ul style="list-style-type: none"> The tax base under the new tax measures is the ‘international minimum tax amount’ which is the sum of the amounts calculated using the following method: [X] × [Attribution ratio calculated by considering the ownership interest of the Japanese companies, etc. ^{(*)1}] Above [X] means as follows: The ‘international minimum tax amount by company, etc.’ allocated to other constituent companies, etc.^{(*)2} of the Specified MNE Group, etc. or joint ventures^{(*)2} related to the Specified MNE Group, etc., out of the top-up tax amount of the Specified MNE Group, etc. to which the Japanese company belongs as a constituent company, etc. <p>^{(*)1} Where Japanese companies own the shares in constituent companies, etc. through intermediate parent entities, etc. or partially-owned parent entities, etc., top-up tax will be reduced by the amount of the top-up tax attributable to the intermediate parent companies, etc. or partially-owned parent entities, etc.</p> <p>^{(*)2} Excluding constituent companies, etc. and joint ventures located in Japan</p>

The following shows an image of the calculation of ‘international minimum tax amount’ in the following case^(*):

- The ETR by country where the constituent companies, etc. are located is below 15% (base tax rate) and
- There is group net income in the country where the constituent companies, etc. are located.

(*) Please note there are certain cases where top-up tax is imposed, even if there is no amount of group net income by country where the constituent companies, etc. are located.



- Substance-based income exclusion:
The sum of the payroll carve-out and tangible asset carve-out which are certain percentages of payroll costs and the carrying value of tangible assets
- Additional current top-up tax:
Adjustment to the top-up tax where the recalculation of prior years' top-up tax results in an adjustment being required in the current fiscal year, etc.

(ii) Exemption

Where constituent companies, etc. of the Specified MNE Group, etc. satisfy all of the following conditions for each applicable fiscal year, the 'international minimum tax amount by country for applicable fiscal year' (please refer to the figure in (i)) of the country where the constituent companies, etc. are located will be treated as zero:

(a)	The average of income of the Specified MNE Group, etc. for the applicable fiscal year and the two applicable fiscal years immediately preceding the first mentioned applicable fiscal year in the country where the constituent companies, etc. are located is less than the amount equivalent to EUR10 million.
(b)	The average profit or loss of the Specified MNE Group, etc. for the applicable fiscal year and the two applicable fiscal years immediately preceding the first mentioned applicable fiscal year in the country where the constituent companies, etc. are located is less than the amount equivalent to EUR1 million.

- The exemption for joint ventures will be basically the same as that for constituent companies, etc.
- A transitional exemption rule using certain items stated in country-by-country reporting and other necessary measures will be provided.

(iii) Calculation of tax amount, filing and tax payment, etc.

■ Calculation of tax amount

The 'corporation tax on international minimum tax amount for each applicable fiscal year' will be calculated as follows:

$$\text{The 'corporation tax on international minimum tax amount for each applicable fiscal year'} = [\text{international minimum tax amount for each applicable fiscal year}] \times 90.7\%$$

■ Filing and tax payment

- A Japanese company belonging to the Specified MNE Group, etc. is required to file a tax return and pay the 'corporation tax on international minimum tax amount for each applicable fiscal year' within one year and three months (one year and six months in certain cases) from the day following the end of each applicable fiscal year. (However, if there is no 'international minimum tax amount', the filing is not required.)
- Electronic filing will be required (the same as for the corporation tax on income).
- Other necessary measures will be provided.

■ Others

- The 'corporation tax on international minimum tax amount for each applicable fiscal year' will not be subject to the blue-form tax return system.
- The rights of question and inspection of the tax authority and penalties, etc. will be treated in the same manner as the corporation tax on income.
- Other necessary measures will be provided.

(iv) Timing of application

The 'corporation tax on international minimum tax amount for each applicable fiscal year' will be applied to Japanese companies for applicable fiscal years beginning on or after 1 April 2024.

(3) Establishment of new tax measures for ‘local corporation tax on specified standard corporation tax amount’

In line with the establishment of the ‘corporation tax on international minimum tax amount for each applicable fiscal year’, the ‘local corporation tax on specified standard corporation tax amount’ (national tax) will also be imposed for each applicable fiscal year on Japanese companies belonging to the Specified MNE Groups, etc.

(i) Calculation of tax amount, filing and tax payment, etc.

■ Calculation of tax amount

The ‘local corporation tax on specified standard corporation tax amount’ will be calculated as follows:

$$\text{The ‘local corporation tax on specified standard corporation tax amount’} = [\text{‘specified standard corporation tax amount’ for the applicable fiscal year}] \times 93 / 907$$

The ‘specified standard corporation tax amount’ is defined as the amount of ‘corporation tax on the international minimum tax for each applicable fiscal year’ excluding penalty taxes.

■ Filing and tax payment

- The ‘local corporation tax on specified standard corporation tax amount’ requires filing of a tax return and payment of the tax within one year and three months (one year and six months in certain cases) from the day following the end of each applicable fiscal year.
- Electronic filing will be required (the same as for the local corporation tax on corporation tax).
- Other necessary measures will be provided.

■ Others

- The rights of question and inspection of the tax authority and penalties, etc. will be treated in the same manner as the local corporation tax on corporation tax.
- Other necessary measures will be provided.

(ii) Timing of application

The ‘local corporation tax on specified standard corporation tax amount’ will be applied to Japanese companies for applicable fiscal years beginning on or after 1 April 2024.

(4) Establishment of information declaration system

(i) Outline

A Japanese company which is a constituent company, etc. of the Specified MNE Group, etc. must provide certain information related to the Specified MNE Group, etc. (e.g. the name of the constituent companies, etc. of the Specified MNE Group, etc., and the ETR by country where the constituent companies, etc. are located, etc.) in English via e-Tax to the competent tax office within one year and three months (one year and six months in certain cases) from the day after the end of each applicable fiscal year.

If there are two or more Japanese companies that are required to provide certain information related to the Specified MNE Group, etc., it will be sufficient that one company representing such Japanese companies provides such information.

(ii) Exemption from filing obligation

Where the tax authority of the country where the ultimate parent company, etc. of the Specified MNE Group, etc. (in cases where one constituent company is designated by the ultimate parent company, etc., the designated company will be substituted.) is located is able to provide Japan with the information regarding the Specified MNE Group, etc., the Japanese company that is obligated to provide such information will be exempted from such obligation.

However, a Japanese company which is exempted from the obligation to provide such information must provide the notification regarding the ultimate parent company, etc. to the competent tax office by e-Tax within one year and three months (one year and six months in certain cases) from the day following the end of each applicable fiscal year.

If there are two or more Japanese companies that are required to provide the notification regarding the ultimate parent company, etc., it will be sufficient that one company representing such Japanese companies provides such notification.

(iii) Timing of application

The above new measures will be applied to 'corporation tax on international minimum tax amount' for applicable fiscal years of Japanese companies beginning on or after 1 April 2024.

In accordance with the new measures to (2) through (4) above, other necessary measures will be provided.

2. Controlled Foreign Company (CFC) Regime

Corresponding to the introduction of the new tax measures of the GloBE Rule of ‘Pillar 2’ under the 2023 tax reform indicated in ‘1. GloBE Rule - Income Inclusion Rule’ above, the following amendments and other necessary measures related to the controlled foreign company (‘CFC’) regime will be provided taking into account the additional administrative burden for companies subject to the new tax measures:

(1) Amendment to threshold effective tax rate for full-inclusion rules of Specified CFC

Where the effective tax rate (‘ETR’) of the foreign subsidiary that falls under the ‘Specified CFC’ (Paper Company, Cash Box and Black-List Company) is under 30 percent, the income of the ‘Specified CFC’ for a fiscal year with certain adjustments should be included in its Japanese shareholders’ income (full-inclusion rule).

By virtue of the 2023 tax reform, the threshold ETR for the full-inclusion rule will be reduced to 27 percent.

[Current tax law]

Classification of CFC		ETR		
		Under 20%	20% or more & under 30%	30% or more
Specified CFC (Paper Company, Cash Box and Black-List Company)		Full-inclusion		No income inclusion
Other than Specified CFC	Full-Inclusion CFC (At least one of the Economic Activity Tests is not satisfied.)	Full-inclusion		
	Partial-Inclusion CFC (All of the Economic Activity Tests are satisfied.)	Partial-inclusion		

[Proposal]

Classification of CFC		ETR		
		Under 20%	20% or more & under 27%	27% or more
Specified CFC (Paper Company, Cash Box and Black-List Company)		Full-inclusion		No income inclusion
Other than Specified CFC	Full-Inclusion CFC (At least one of the Economic Activity Tests is not satisfied.)	Full-inclusion		
	Partial-Inclusion CFC (All of the Economic Activity Tests are satisfied.)	Partial-inclusion		

(2) Amendments to attachments to tax returns

(i) Scope of documents related to foreign subsidiary

The documents related to the following Partial-Inclusion CFC (foreign subsidiary subject to the partial-inclusion rule of passive income) will be excluded from the scope of the documents related to a foreign subsidiary which are currently required as the attachments to the tax returns and those documents will be required to be preserved instead:

- Partial-Inclusion CFC with no partial-inclusion amount (amount subject to partial-inclusion rule before multiplying by the shareholding ratio)
- Partial-Inclusion CFC exempted from the CFC regime by satisfying the requirements for exemption, such as JPY20 million or less of the partial-inclusion amount, etc.

(ii) Matters to be stated in documents related to foreign subsidiary

Regarding the matters to be stated in the documents related to a foreign subsidiary which are required as the attachments to the tax returns (limited to the documents stating matters related to shareholders, etc. who directly or indirectly hold shares, etc. in the foreign subsidiary), it will be allowed to state all or part of such matters in a diagram which systematically shows the relationship between the foreign subsidiary and its shareholders, etc., instead of such documents.

Above amendments will be applied to fiscal years beginning on or after 1 April 2024 for the Japanese shareholder company.

Note that necessary measures will also be provided for corporate inhabitant tax and corporate business tax purposes in line with the above amendments.

Further amendments will be examined under the 2024 tax reform or after corresponding to the enactment of the GloBE Rule of 'Pillar 2.'

III. Income Taxation

Fair Tax Burden on Extremely High-Level Income

It is statistically said that the national income tax burden ratio of wealthy individuals who have a large amount of asset income derived from stocks or land, etc., which are subject to separate taxation at a flat rate, decreases when their income reaches JPY100 million. In order to deal with the so-called "JPY100 million barrier," from the perspective of fairness of the tax burden, a new tax measure will be established which requires a minimum tax burden for extremely high-level income.

Specifically, national income tax calculated by the following formula will be imposed:

$$([\text{Amount of Standard Taxable Income for the year}] - [\text{JPY330 million}]) \times 22.5\% - [\text{Amount of Standard National Income Tax for the year}]$$

[Definition of key terms]

<p>Amount of Standard Taxable Income</p>	<p>Amount of total income (goukei-shotoku-kingaku)^(*) of the national income tax calculated without consideration of the No-declaration System for the year (after the special deduction applied to national income tax for the year)</p> <p>^(*) Amount of total income (goukei-shotoku-kingaku) does not include the following:</p> <ul style="list-style-type: none"> • The amount of income subject to separate declaration taxation system • The amount exempted from taxation under the NISA system and the special provisions for the deduction of the amount of acquired shares that specified small and medium-sized companies issued at their establishment
<p>No-declaration System</p>	<p>The following special provisions:</p> <ul style="list-style-type: none"> • Special provisions for dividend income, etc., which do not require filing of final national income tax return • Special provisions for income from transfer of listed shares, etc., which do not require filing of final national income tax return
<p>Amount of Standard National Income Tax</p>	<p>Amount of national income tax imposed on the Amount of Standard Taxable Income for the year</p> <p>(The amount of national income tax is the amount before applying foreign tax credits, etc. and excludes penalty taxes and the amount of national income tax imposed by the tax measure.)</p>

Note that the items to be stated in the final national income tax return for the application of the tax measure will be prescribed and other necessary measures will also be provided.

The above amendment will apply for national income tax from 2025.

IV. Improvements in Tax Administration Matters

1. Electronic Preservation System for Account Books, etc.

In order to enhance digitalization of national tax-related account books and documents, the following amendments and other necessary measures will be introduced:

(1) Preservation system for national tax-related account books and documents by electromagnetic records

Where the preservation obligor files an amended tax return or receives a reassessment on income tax (excluding withholding income tax), corporation tax or consumption tax related to the matters of the electromagnetic records in the so-called “excellent national tax-related account books,” the rate of additional tax for understatement levied on the omission of the declaration related to such recorded matters is reduced by 5 percent.

The ‘excellent national tax-related account books’ are those that satisfy certain preservation requirements for maintenance and preservation of electromagnetic records in the special national tax-related account books (for which a preservation obligor has submitted a certain application form to the competent tax office in advance of applying the reduction in the rate of additional tax for understatement related to the matters of the electromagnetic records in the special national tax-related account books, etc.).

In order to achieve a greater shift to reliable electronic account books, the scope of the ‘excellent national tax-related account books’ related to income tax (excluding withholding income tax) and corporation tax will be amended as follows:

Current tax law	Proposal
<ul style="list-style-type: none"> • Journals • General ledger • Other necessary books 	<ul style="list-style-type: none"> • Journals • General ledger • Account books, other than journals and general ledger, for the records of the following matters (except for the matters listed in (iv) for ‘excellent national tax-related account books’ for income tax (excluding withholding income tax) purposes) <ul style="list-style-type: none"> (i) Matters related to notes receivable and notes payable (excluding accommodation bills) (ii) Matters related to accounts receivable (including accrued processing fees and other items similar in nature to accounts receivable) and other receivables (excluding matters related to deposits and withdrawals from checking accounts) (iii) Matters related to accounts payable (including accrued processing fees and other items similar in nature to accounts payable) and other payables (iv) Matters related to securities (excluding those that are commodities) (v) Matters related to depreciable assets (vi) Matters related to deferred assets

	<p>(vii) Matters related to sales (including processing, other services rendered and other items of a similar nature to sales, etc.) and other income</p> <p>(viii) Matters related to purchases and other expenses or costs (excluding wages, salary allowances, legal welfare expenses and welfare expenses in the case of 'excellent national tax-related account books' for corporation tax purposes)</p>
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The above amendments will be applied to national tax for which the statutory tax return filing due date is on or after 1 January 2024.

(2) Scanner preservation system

National tax-related documents, except for book closing documents, can be preserved as electromagnetic records recorded by a scanner under certain preservation requirements in lieu of preservation of such documents.

From the perspective of promoting the use of the system, the following requirements of the scanner preservation system will be abolished or mitigated:

Requirements	Proposal
Preservation of information about resolution, gradation and size	The requirement of the preservation of information about resolution, gradation and size of scanned national tax-related documents will be abolished.
Confirmation of information about input person, etc.	The requirement of the confirmation of information about input person, etc. of the recorded matters related to the national tax-related documents will be abolished.
Inter-relationship between scanned documents and national tax-related account books	The documents, which are required to be able to confirm the inter-relationship between scanned documents and recorded items of the national tax-related account books, will be limited to important documents such as contracts and receipts, etc.

The above amendments will be applied to national tax-related documents that are preserved on or after 1 January 2024.

(3) Preservation system for electromagnetic records related to transaction information of electronic transactions

Where a preservation obligor regarding income tax (excluding withholding income tax) and corporation tax carries out electronic transactions in which transaction information is exchanged by electromagnetic methods, the transaction information must be preserved by electromagnetic records in accordance with certain preservation requirements. This preservation system will be amended as follows:

(i) Amendments to the preservation requirements

(a) Requirement for ensuring search functionality

The requirement for ensuring search functionality, which is the one of the requirements for the preservation system for electromagnetic records

related to transaction information of electronic transactions, will be amended as follows:

[Current law]

■ Principle

All of the following requirements must be satisfied:

(a)	Transaction date and other dates, transaction amount and counterparty ('search items') can be set as search conditions.		
(b)	Search conditions can be set for search items of dates or amounts by designating the scope.	←	[Special provision for download request] Where the preservation obligor follows the request for download of electromagnetic records by the National Tax Agency, etc. based on its rights of question and inspection, (b) and (c) on the left are not required.
(c)	Search conditions can be set by combining two or more search items arbitrarily.	←	

■ Special provisions for preservation obligor with low sales

Where a preservation obligor satisfies both of the following conditions, the requirements for ensuring a search functionality are not applied.

(a)	Sales amount during the determination period ^(*) ≤ JPY10 million
(b)	The preservation obligor follows the request for download of electromagnetic records by the National Tax Agency, etc. based on its rights of question and inspection

^(*) In the case of a company, the fiscal year prior to the first preceding fiscal year of the fiscal year including the day on which the electronic transaction was made

[Proposal]

From the perspective of promoting the preservation of electromagnetic records that are identical to electronic data received from other parties, the conditions, by which the requirements for ensuring search functionality are not applied, will be amended as follows:

Amendment to [Special provision for download request] in 'Principle'	<p><u>Where a 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 and organized by transaction date and counterparty) by the National Tax Agency, etc. and request for download of electromagnetic records by the National Tax Agency, etc. based on its rights of question and inspection, all of the requirements for ensuring search functionality will not be applied.</u></p>
Amendment to 'Special provisions for preservation obligor with low sales'	<p>The requirement of (a) in the above will be amended as follows: Sales amount during the determination period ≤ <u>JPY50 million</u></p>

(b) Requirement for time stamping

Among the requirements for time stamping, the requirement that "a preservation obligor must make it possible to confirm the information

about the person who preserves the electromagnetic records, etc.' will be abolished.

(ii) Amendments to measure for preserving output documents of electromagnetic records

By virtue of the 2021 tax reform, the measure that allows the preservation of output documents created by outputting electromagnetic records related to transaction information of electronic transaction was abolished. Thereafter, the transitional measure was established under the 2022 tax reform that allows the preservation of output documents until 31 December 2023 as far as certain requirements are satisfied.

The Proposal states that the transitional measure will end on 31 December 2023 as prescribed in the current law and the following measure will be newly provided for companies/business persons that are not able to prepare for the necessary system with reasonable grounds:

Transitional measure which will end on 31 December 2023	Proposed measure under the 2023 tax reform
<p>A preservation obligor regarding income tax (excluding withholding income tax) and corporation tax can preserve output documents instead of preserving electromagnetic records related to transaction information for electronic transactions until 31 December 2023, as far as the following conditions are satisfied:</p> <p><Conditions></p> <ul style="list-style-type: none"> • The competent tax office acknowledges <u>unavoidable grounds</u> for the failure of the preservation of the electromagnetic records related to transaction information of electronic transactions in compliance with the preservation requirements. • 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. 	<p>A preservation obligor regarding income tax (excluding withholding income tax) and corporation tax will be able to preserve electromagnetic records related to transaction information for electronic transactions regardless of the preservation requirements as far as the following conditions are satisfied:</p> <p><Conditions></p> <ul style="list-style-type: none"> • The competent tax office acknowledges <u>reasonable grounds</u> for the failure of the preservation of the electromagnetic records related to transaction information of electronic transactions in compliance with the preservation requirements. • The preservation obligor follows the <u>request for downloading of the electromagnetic records related to transaction information of electronic transactions</u> and 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 amendments in (3) above will be applied to electromagnetic records related to transaction information of electronic transactions that are conducted on or after 1 January 2024.

In local taxes, as with national taxes, necessary measures will be provided with respect to the requirements for electronic preservation of documents, etc. related to the local tobacco tax and the diesel oil delivery tax, etc.

V. Tax Measures to Secure Financial Resources for Strengthening Defense Capability

In order to secure financial resources for the drastic strengthening of Japan's defense capability, the implementation of tax measures is planned in phases over multiple years toward 2027.

The following tax measures will be implemented at an appropriate time after 2024.

1. Corporation Tax

A new additional tax calculated by the following formula will be imposed:

In consideration of small and medium-scale companies, JPY5 million will be deducted from the amount of corporation tax as the tax base.

Additional corporation tax = $([\text{Corporation tax liability}] - [\text{JPY5 million}]) \times 4\sim 4.5\%$

2. Income Tax

(1) Additional Tax

For the time being, a new additional tax at the rate of 1 percent will be imposed on the amount of income tax.

(2) Special Reconstruction Income Tax

In order to secure the financial resources necessary for measures for reconstruction from the Great East Japan Earthquake, the special reconstruction income tax is imposed at the rate of 2.1 percent on the amount of standard national income tax as the tax base from 1 January 2013 to 31 December 2037.

In consideration of the current situation surrounding household finances, the special reconstruction income tax rate will be reduced by 1 percent from 2.1 percent to 1.1 percent and the taxation period will be extended.

The extension period will be the length necessary to ensure that the total amount of reconstruction financial resources is secured so as not to affect the steady implementation of reconstruction projects related to the Great East Japan Earthquake.

3. Tobacco Tax

While giving due consideration to the impact to domestic leaf tobacco farmers and ensuring predictability, an increase equivalent to JPY3 per cigarette will be implemented in phases.

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