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Tax Update

NATIONAL TAX AGENCY — EXPLANATION OF THE ADMINISTRATIVE GUIDANCE RELATED TO THE JAPANESE IIR

By virtue of the 2024 tax reform, the Japanese Income Inclusion Rule (hereinafter 'J-IIR'), which is equivalent to the Income Inclusion Rule ('IIR') of the Global Minimum Tax in Pillar 2 agreed by the OECD/G20 Inclusive Framework on BEPS and which was established in the 2023 tax reform, was amended from the perspective of clarifying the rules based on the content of the administrative guidance issued by the OECD and international discussions, etc.

On 8 November 2024, the National Tax Agency released the explanation of the administrative guidance, which was issued on 5 August 2024^(*) (hereinafter 'Explanation of AG', Japanese only) corresponding to the amendments to the J-IIR under the 2024 tax reform.

The Explanation of AG explains the administrative guidance (hereinafter 'New AG') and transitional treatments, which were newly provided in the administrative guidance above and, for example, includes the following explanations.

<Amount of specified expenses in the case where the employee's working ratio in the country, where the constituent companies, etc. are located, exceeds 50 percent>

By virtue of the 2024 tax reform, the calculation method of specified expenses (i.e. salaries, etc. for employees) regarding the substance-based income exclusion are clarified in the case where employees, etc. of the constituent companies, etc. work in multiple countries including the country where the constituent companies, etc. are located.

Considering the Japanese corporation tax laws/regulations and the OECD administrative guidance issued in July 2023, the New AG clarifies that the amount of specified expenses must be calculated without taking into account the employee's working ratio in the country, where the constituent companies, etc. are located, in the case where the employee's working ratio exceeds 50 percent.

In addition, the New AG indicates that it is acceptable to determine whether the employee's working ratio in the country, where the constituent companies, etc. are located, exceeds 50 percent based on the provisions of the work rules, labor contracts or 'other similar documents'

(hereinafter 'Work Rules, etc.') in the case where the Work Rules, etc. of the constituent companies, etc. specify the working place and period of the employees, etc. and the work of employees is deemed to be performed in accordance with the provisions of the Work Rules, etc.

The Explanation of AG explains that the 'other similar documents' above include labor agreements between the constituent companies, etc. and a labor union to which the employees of the constituent companies, etc. belong, or contract work agreements between the constituent companies, etc. and the independent contractor who is engaged in the ordinary business of the constituent companies, etc. (limited to business performed under the direction and command of the constituent companies, etc. or other constituent companies, etc. of the specified multinational group, etc. to which the constituent companies, etc. belong).

<Where the 'financial statements in the country of residence' are not prepared>

By virtue of the 2024 tax reform, the QDMTT Safe Harbour was established, which allows the jurisdictional top-up tax in the country, where constituent companies, etc. in the specified multinational group, etc. are located, to be treated as zero for the applicable fiscal year as long as the constituent companies, etc. are subject to the QDMTT that satisfies the QDMTT Accounting Standard and the Consistency Standard in the jurisdiction other than Japan.

The QDMTT Accounting Standard above requires that the tax laws/regulations related to the QDMTT satisfy certain conditions and the New AG clarifies the treatment of the 'case where the financial statements in the country of residence of any member company of the specified multinational group, etc. are not prepared' among those conditions.

The Explanation of AG indicates that the case where financial statements are not prepared in accordance with the financial accounting standards of the country of residence, is also treated as the 'case where the financial statements in the country of residence of any member company of the specified multinational group, etc. are not prepared'.

(*) We set out an outline of the administrative guidance in the e-Tax News No.314 ['Administrative Guidance for the J-IIR'](#) issued on 19 August 2024.

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