

KPMG Japan Tax Newsletter

18 November 2016



CONSUMPTION TAX

INTRODUCTION OF REDUCED TAX RATE & INVOICING SYSTEM

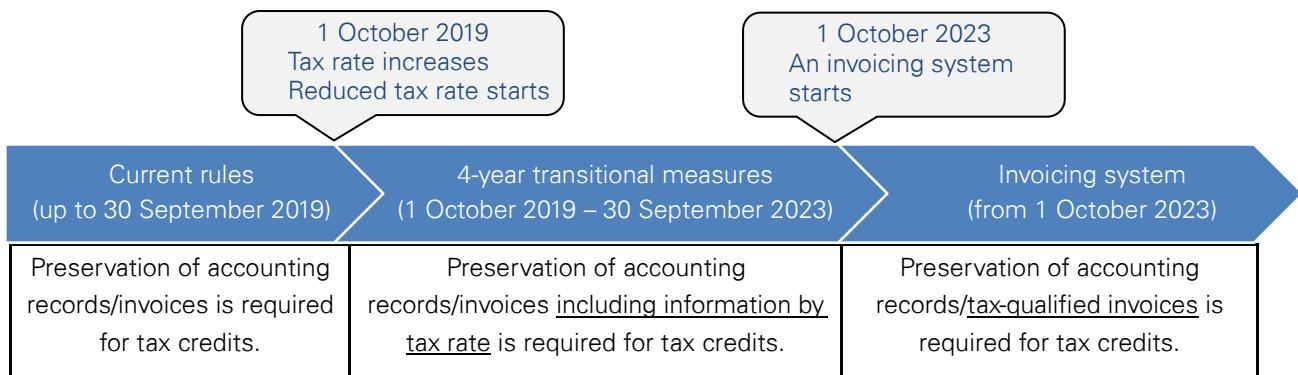
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On 18 November 2016, the bills to postpone the consumption tax rate increase by two and a half years were passed by the extraordinary session of the Japanese Diet, thereby delaying the consumption tax rate increase from 8 percent until 10 percent on 1 October 2019. A multiple tax rate system where the reduced tax rate of 8 percent will be applied to certain transactions including sales of food/beverages will also be introduced along with the increase in the consumption tax rate. Furthermore, an invoicing system will be introduced so that the creditable tax amount can be calculated properly under the multiple tax rate system. However, this will start on 1 October 2023, i.e. 4 years after the introduction of the multiple tax rate system, considering the fact that businesses need a time to prepare for the new system.

We have set out below a brief summary of transactions subject to the reduced tax rate, details of the invoicing system and the 4-year transitional measures.

I. Time Schedule of Revisions

The illustration below shows the timing of the revisions and changes in the requirements for tax credits:



II. Introduction of Reduced Tax Rate

1. Consumption tax increase and introduction of reduced tax rate

up to 30 September 2019	from 1 October 2019	
8% National: 6.3% Local: 1.7%	<ul style="list-style-type: none"> Sales of food and beverages Sales of newspapers under subscription contracts 	8% National: 6.24% Local: 1.76%
	Other than the above	10% National: 7.8% Local: 2.2%

The consumption tax rate was originally planned to increase from 5 percent to 8 percent on 1 April 2014 and from 8 percent to 10 percent on 1 October 2015. Although the increase from 5 percent to 8 percent was implemented as originally planned, the increase from 8 percent to 10 percent has been postponed for 4 years in total, as it had already been postponed by one and a half years before the second postponement determined by the extraordinary session of the Diet in November 2016.

There is a transitional measure for the consumption tax rate increase where 8 percent will continuously be applied to transactions under certain conditions on or after 1 October 2019. Where certain transactions (e.g. the sale of goods through mail-order sales) subject to that transitional measure are also subject to the reduced tax rate, the reduced tax of 8 percent (national: 6.24 percent, local: 1.76 percent) will be applied to such transactions.

2. Transactions subject to reduced tax rate

The reduced tax rate will be applied to the following transactions:

(1) The sale of food and beverages	
Food and beverages	<p>'Food' defined under the Food Labeling Act (excluding alcoholic drinks)</p> <p>Food sold together with goods other than food as one combined product, meeting the following conditions:</p> <ul style="list-style-type: none"> • The price of the product is less than JPY10,000. • 2/3 or more of the price of the product relates to food.
The sale of food and beverages	<p>Excludes:</p> <ul style="list-style-type: none"> • The provision of meals by certain business operators (e.g. business operators conducting restaurant businesses or coffee shop businesses) at places equipped with eating facilities • The provision of meals through catering services <p>Includes:</p> <ul style="list-style-type: none"> • The sale of boxed meals for customers to take home • Certain provision of meals at homes for elderly people, kindergartens and elementary /junior high schools, etc.
(2) The sale of newspapers under subscription contracts (provided that the newspapers contain articles with respect to politics, economy, social affairs and culture, etc. and are issued at least twice a week)	

In addition, importation of food and beverages will be subject to the reduced tax rate as well.

III. 4-Year Transitional Measures

The following transitional measures have been set up for the 4-year period from 1 October 2019 (when the reduced tax rate system starts) to 30 September 2023 (when an invoicing system starts.)

1. Requirements for tax credits

Under the current tax rules, it is necessary to preserve 'accounting records' and 'invoices' describing certain items in order to take tax credits for taxable purchases. In the 4-year transitional period, the underlined parts below will be added to the items to be described in 'accounting records' and 'invoices'.

Items to be described in 'accounting records'
(a) Name of the supplier
(b) Date of the taxable purchases
(c) Description of the taxable purchases <u>(if they are subject to the reduced tax rate, a statement to clarify that fact should also be included.)</u>
(d) Consideration for the taxable purchases

Items to be described in 'invoices'
(a) Name of the supplier
(b) Date of the taxable supplies
(c) Description of the taxable supplies <u>(if they are subject to the reduced tax rate, a statement to clarify that fact should also be included.)</u>
(d) Consideration for the taxable supplies (incl. tax) <u>by tax rate</u>
(e) Name of the purchaser

- 'Invoices' for certain transactions (e.g. transactions less than JPY30,000, purchases through automatic vending machines, admission tickets, train tickets) are not required to be preserved. (Same treatment as under the current rules)
- (e) can be omitted for certain kinds of business providing taxable supplies to many and unspecified persons (e.g. retail business, eating and drinking business, taxi business and automobile parking business). (Same treatment as under the current rules)
- The purchaser can add by themselves the underlined parts of (c) and (d) in the invoices.
- 'Invoices' include not only documents issued by the supplier (e.g. billing statements, receipts) but also documents prepared by the purchaser (e.g. purchase statements) that are authorized by the supplier. (Same treatment as under the current rules)

(Note that the above "Items to be described in 'invoices'" indicate those to be described in documents issued by the supplier.)

2. Special measures for small and medium-sized businesses

Considering cases where small and medium-sized businesses have difficulty in identifying taxable sales/purchases by tax rate in the 4-year transitional period, special calculation methods have been set up for small and medium-sized businesses.

Taxable persons can choose one of the following two special calculation methods for taxable sales:

	Eligible persons	Applicable periods	Brief description
Method 1	Taxable persons who have difficulty in identifying total taxable sales by tax rate	All of the following are met: <ul style="list-style-type: none"> • Taxable sales for the base period (generally, the fiscal year 2 years prior to the current fiscal year) do not exceed JPY50 million. • From 1 October 2019 to 30 September 2023 	Calculation by using the ratio of (2)/(1) ^(*) <ul style="list-style-type: none"> (1) Taxable sales (incl.tax) for 10 successive ordinary business days (2) Taxable sales (incl.tax) subject to the reduced tax rate for 10 successive ordinary business days
Method 2	Taxable persons who have difficulty in identifying total taxable sales for wholesale and retail business by tax rate	All of the following are met: <ul style="list-style-type: none"> • Taxable sales for the base period do not exceed JPY50 million. • The simplified tax credit system is not applied. • From 1 October 2019 to 30 September 2023 	Calculation by using the ratio of (2)/(1) ^(*) <ul style="list-style-type: none"> (1) Taxable purchases (incl.tax) required only for wholesale and retail business (2) Taxable purchases (incl.tax) subject to the reduced tax rate required only for wholesale and retail business

(*) If it is difficult for taxable persons whose main business is taxable supplies subject to the reduced tax rate to calculate the proportion, 50 percent will be applicable instead of the proportion of (2)/(1).

Taxable persons can choose one of the following two special calculation methods for taxable purchases. Please note however, that neither of them will be applicable when method 2 is chosen for the calculation of taxable sales by tax rate.

	Eligible persons	Applicable periods	Brief description
Method 1	Taxable persons who have difficulty in identifying total taxable purchases for wholesale and retail business by tax rate	All of the following are met: <ul style="list-style-type: none"> • Taxable sales for the base period do not exceed JPY50 million. • The simplified tax credit system is not applied. • From 1 October 2019 to the end of the taxable period which includes 30 September 2020 	Calculation by using the ratio of (2)/(1) <ul style="list-style-type: none"> (1) Taxable sales (incl.tax) for wholesale and retail business (2) Taxable sales (incl.tax) for wholesale and retail business subject to the reduced tax rate

Method 2	Taxable persons who have difficulty in identifying total taxable purchases by tax rate	All of the following are met: <ul style="list-style-type: none">• Taxable sales for the base period do not exceed JPY50 million.• The simplified tax credit system is not applied.• Taxable periods with days between 1 October 2019 and 30 September 2020	Where an application form for the simplified tax credit system is submitted by the end of the applicable period, the simplified tax credit system will be applied for the taxable period of the submission onwards.
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Although special measures similar to the above have also been prepared for large taxpayers considering cases where it takes time to make appropriate changes to their operating systems, such measures were abolished since there should be sufficient time to change such operating systems due to the postponement of the introduction of a multiple tax rate system.

IV. Invoicing System

An invoicing system adopted broadly in European countries will be introduced on 1 October 2023 so that the creditable tax amount can be calculated properly under the multiple tax rate system. Preservation of 'tax-qualified invoices' issued by registered suppliers will be one of requirements for tax credits.

1. Registered suppliers to issue tax-qualified invoices

■ Registration system

A new system for registered supplier who are eligible to issue 'tax-qualified invoices' or 'tax-qualified simplified invoices' will be set up. An outline of the system is as follows:

Registration	<p>A taxable person will be registered as a registered supplier who is eligible to issue 'tax-qualified invoices' by submitting an application form to the competent tax office.</p> <p>(Application should be submitted by 31 March 2023 to be registered by 1 October 2023.)</p>
	<p>In the case of partnerships (e.g. Nini-Kumiai (NK)), where all of partners of a partnership are registered suppliers, a managing partner can issue 'tax-qualified invoices.'</p> <p>(Submission of a special application should be required.)</p>
Registered suppliers list	<p>Information on registered suppliers (e.g. name and identification number) will be made public on the National Tax Agency website immediately after the registration.</p>
Tax exempt status	<p>A registered supplier will not be able to have tax exempt status after the registration unless its registration is canceled.</p>
Registered foreign suppliers	<p>Under the current rules, there is a registration system for foreign suppliers who provide B2C digital services. Registered foreign suppliers as of 1 September 2023 will be treated as being registered as registered suppliers who are eligible to issue 'tax-qualified invoices' on 1 October 2023.</p>

■ What registered suppliers must do

A registered supplier has an obligation to issue and preserve 'tax-qualified invoices' or 'tax-qualified simplified invoices' as follows:

Obligation to issue tax-qualified invoices	[In principle] Registered suppliers are required to issue 'tax-qualified invoices' upon requests from the counterparties of taxable supplies. (Items to be described in 'tax-qualified invoices' can be provided electronically instead of in 'tax-qualified invoices,' where advance acknowledgement is obtained from the counterparties.)
	[Exceptions] Where registered suppliers conduct certain kinds of business providing taxable supplies to many and unspecified persons (e.g. retail business, eating and drinking business, taxi business and automobile parking business), such suppliers will be able to issue 'tax-qualified simplified invoices' instead of 'tax-qualified invoices'.
Exempt from obligation to issue tax-qualified invoices	Registered suppliers are not required to issue 'tax-qualified invoices' and 'tax-qualified simplified invoices' for certain taxable supplies including the following: <ul style="list-style-type: none"> • The provision of public transportation services (ships, buses and railways) provided that the consideration is less than JPY30,000 • The supply through automatic vending machines provided that the consideration is less than JPY30,000 • Certain taxable supplies where it is difficult to issue tax-qualified invoices
Obligation for preservation	Registered suppliers are required to preserve copies of 'tax-qualified invoices' and 'tax-qualified simplified invoices.'

■ Prohibited acts and penalties

Issuance of the following documents are prohibited and penalties (imprisonment for up to 1 year or a fine of up to JPY500,000) will be imposed on persons who violate such prohibition.

Persons who are not registered suppliers	Documents which may lead recipients to misunderstand that they are 'tax-qualified invoices' or 'tax-qualified simplified invoices'
Registered suppliers	'Tax-qualified invoices' or 'tax-qualified simplified invoices' including false information

2. Tax-qualified invoices

The following items should be described in 'tax-qualified invoices' and 'tax-qualified simplified invoice.' The underlined parts below will be added to the items to be described in 'invoices' under the current rules.

Items to be described in 'tax-qualified invoices'	Items to be described in 'tax-qualified simplified invoices'
(a) Name and <u>identification number</u> of the registered supplier	(a) Name and <u>identification number</u> of the registered supplier
(b) Date of the taxable supplies	(b) Date of the taxable supplies
(c) Description of the taxable supplies <u>(if they are subject to the reduced tax rate, a statement to clarify that fact should also be included.)</u>	(c) Description of the taxable supplies <u>(if they are subject to the reduced tax rate, a statement to clarify that fact should also be included.)</u>
(d) Consideration for the taxable supplies <u>(excl. or incl. tax) by tax rate and applicable tax rates</u>	(d) Consideration for the taxable supplies <u>(excl. or incl. tax) by tax rate</u>
(e) <u>Amount of consumption tax</u>	(e) <u>Amount of consumption tax or applicable tax rates</u>
(f) Name of the purchaser	

3. Requirements for tax credits

Under the invoicing system, it is necessary to preserve 'accounting records' and 'invoices' (e.g. 'tax-qualified invoices') describing certain items in order to take tax credits for taxable purchases.

The items to be described in 'accounting records' are as follows. These are the same as those required in the 4-year transitional period, i.e. the underlined parts below will be added to the items to be described in 'accounting records' under the current rules.

Items to be described in 'accounting records'
(a) Name of the supplier
(b) Date of the taxable purchases
(c) Description of the taxable purchases <u>(if they are subject to the reduced tax rate, a statement to clarify that fact should also be included.)</u>
(d) Consideration for the taxable purchases

The scope of 'invoices' to be preserved is as follows:

Scope of 'invoices' (main items)
<ul style="list-style-type: none"> • 'tax-qualified invoices' or 'tax-qualified simplified invoices' • electronic information of items to be described in 'tax-qualified invoices' • documents prepared by the purchaser (e.g. purchase statements) including items to be described in 'tax-qualified invoices' provided that they are authorized by the registered suppliers

It is not necessary to preserve 'invoices' to take tax credits for consumption tax paid on certain taxable purchases including the following

- Public transportation services (ships, buses and railways) provided that the consideration is less than JPY30,000
- Documents collected at the time of use such as admission tickets, which meet conditions for 'tax-qualified simplified invoices'
- Taxable purchases through automatic vending machines provided that the consideration is less than JPY30,000
- Certain taxable purchases where it is difficult to receive 'tax-qualified invoices' or 'tax-qualified simplified invoices'

(Under the current rules, it is not required to preserve 'invoices' for taxable purchases whose cost is less than JPY30,000. Such rule will be abolished.)

4. Taxable purchases from non-registered suppliers

As discussed in 3 above, under the invoicing system, preservation of 'tax-qualified invoices' or 'tax-qualified simplified invoices' is one of the requirements for tax credits in principle. However, for the first 6 years, taxable purchases from non-registered suppliers will also be partially subject to tax credits under certain conditions as follows:

Applicable periods	Amount subject to tax credits
From 1 October 2023 to 30 September 2026	80% of consumption tax equivalent on taxable purchases
From 1 October 2026 to 30 September 2029	50% of consumption tax equivalent on taxable purchases

V. Tax-Inclusive Price Labeling Rule

When a taxable person displays prices of goods/services to unspecified and various persons (e.g. price tags and advertisements), they must display tax-inclusive prices under the tax-inclusive price labeling rule. However, the tax-inclusive price labeling rule had been suspended from 1 October 2013 to 30 September 2018 provided that the taxable person takes appropriate measures to prevent people from misunderstanding the displayed prices as tax-inclusive prices from a view point of considering the administrative burden (e.g. changing price tags twice.) The end of such suspension period has been extended by two and a half years to 31 March 2021 as a consequence of the postponement of the consumption tax increase by two and a half years.

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