

KPMG Japan tax newsletter

Introduction of Exit Tax



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Under the 2015 tax reform, special measures to impose income tax on unrealized capital gains on financial assets held by an individual at the time of departure from Japan (exit tax regime) were introduced. The exit tax regime will be applicable from 1 July 2015.

We have set out in this newsletter the outline of the exit tax regime and amendments to the reporting requirement of assets/liabilities which was strengthened due to the introduction of the exit tax.

I. OUTLINE OF THE EXIT TAX REGIME

1. Exit Tax in the case of Departure from Japan

In order to prevent wealthy individuals from avoiding tax on capital gains in Japan by moving out of Japan with appreciated financial assets and subsequently selling those assets, a special measure (exit tax) to impose income tax on unrealized capital gains on financial assets at the time of departure has been introduced.

(1) Eligible person and eligible assets

Eligible person	<p>A resident individual departing from Japan^(*1) and satisfying both of the following conditions:</p> <p>(i) Total amount of the following is JPY100 million or more.</p> <ul style="list-style-type: none"> - The value of eligible assets in (i) below held by the person as of departure from Japan - Profits/losses to be derived from deemed settlements of eligible assets in (ii) below as of departure from Japan <p>(ii) The person has lived in Japan^(*2) for more than 5 years in the last 10 years before departure.</p>	
Eligible assets	(i)	Securities stipulated in the Income Tax Law Contributions under a Tokumei-Kumiai agreement
	(ii)	Unsettled derivatives transactions Unsettled margin transactions Unsettled when-issued transactions (e.g. trading transactions in advance of shares being issued)

(*1) 'Departing from Japan' means to cease to have either domicile or residence in Japan.

(*2) The period of living in Japan includes the grace period described in (5)(ii) below, but excludes the period of staying in Japan with a status of residence under Table 1 of the Immigration Control and Refugee Recognition Act. Furthermore, the period of staying in Japan before 1 July 2015 with a status of residence under Table 2 of the above Act is also excluded from the period of living in Japan as a transitional measure.

As a consequence, the exit tax will not apply to foreign expatriate employees staying in Japan with working visas, such as intra-company transferee or engineer/specialist in humanities/international services under 2 of Table 1. While foreign people staying in Japan with a status of residence under Table 2 (e.g. permanent resident, spouse or child of Japanese national) could be an eligible person, they will not be subject to the exit tax until 1 July 2020 by virtue of the transitional measure.

[Status of residence under the Immigration Control and Refugee Recognition Act]

Table 1	1	Diplomat, Official, Professor, Artist, Religious Activities, Journalist
	2	Highly Skilled Professional, Business Manager, Legal/Accounting Services, Medical Services, Researcher, Instructor, Engineer/Specialist in Humanities/International Services, Intra-company Transferee, Entertainer, Skilled Labor, Technical Intern Training
	3	Cultural Activities, Temporary Visitor
	4	Student, Trainee, Dependent
	5	Designated Activities
Table 2	Permanent Resident, Spouse or Child of Japanese National, Spouse or Child of Permanent Resident, Long-Term Resident	

(Status of residence under Table 1 was amended from 1 April 2015. The above table reflects such amendments.)

(2) Calculation of taxable income

Taxable income (business income, capital gains or miscellaneous income) will be calculated assuming that capital gains/losses on eligible assets were realized at the time of departure from Japan at the following value depending on the case described below:

Cases	Value of the eligible assets as of departure
<ul style="list-style-type: none"> In the case where a notification for appointment of a tax agent is submitted prior to the filing due date of the final income tax return for the year of departure In the case where the final income tax return for the year of departure is filed on or after the date of departure without appointing a tax agent Where a determination is made with respect to the income tax for the year of departure 	The value (or profits/losses to be derived from deemed settlements) of eligible assets as of departure
<ul style="list-style-type: none"> Other than the above 	The value (or profits/losses to be derived from deemed settlements) of the eligible assets as of the day 3 months before the departure (or as of the acquisition date if the eligible assets are acquired after that day)

Note that condition (i) of the eligible person discussed in (1) will also be determined using the above value depending on the case.

(3) Applicable tax rate

The unrealized capital gains will be taxed at 15.315 percent (including special reconstruction income tax) in principle. (Local inhabitant taxes will not be imposed.)

(4) Filing tax returns and tax payments

The eligible person will be required to file their final income tax return to declare unrealized capital gains on eligible assets together with the other income earned in the year of departure and pay income tax by the following due dates:

	Filing due dates	Payment due dates
In the case where a notification for appointment of a tax agent is submitted prior to the departure	15 March of the following year	<ul style="list-style-type: none"> • Where collateral is provided by the filing due date: Grace period for tax payments is applicable (please see (5)(i)-(iv)) • Other than the above: 15 March of the following year
Other than the above	Date of departure	Date of departure

(5) Main points to be considered

The main points to be considered for the measure are as follows:

(i) In the case of returning to Japan within 5 years from departure

- Where an individual who was subject to exit tax returns to Japan within 5 years from the departure, the exit tax on unsold eligible assets will be reversed by filing a request for correction.
- When the grace period (please see (ii) below) is extended to 10 years and the person returns to Japan within 10 years from departure, the above treatment will also be applied.

(ii) Grace period for tax payments

- An individual subject to the exit tax will be allowed to enjoy a tax payment grace period for 5 years (subject to extension upon an application to 10 years) only when all of the following conditions are met:
 - (a) The individual must make an application for the grace period in, and attach certain details to, the final income tax return for the year of the departure.
 - (b) The individual must provide collateral equivalent to the amount of the exit tax subject to the grace period prior to the filing due date of the final income tax return for the year of the departure.
 - (c) The individual must submit a notification for appointment of a tax agent prior to the departure.
- The income tax liability subject to the grace period will be (a) less (b):
 - (a) Income tax liability for the year of departure
 - (b) Income tax liability for the year of departure calculated on the assumption that the exit tax were not imposed
- An individual enjoying the grace period will be required to submit a notification for the eligible assets subject to the grace period held as of 31 December of each year to the competent tax office by 15 March of the following year.
- If the notification is not submitted in time, the grace period will be terminated on the day 4 months after the filing due date.

(iii) In the case where the eligible assets are sold prior to the expiration of the grace period

- The amount of exit tax corresponding to the eligible assets sold within the grace period should be paid within 4 months after the sale.
- Interest tax corresponding to the grace period should also be paid.
- If the selling price of the eligible assets falls below the value of the assets as of the departure, the exit tax will be reduced by filing a request for correction.
- When foreign income tax is imposed on capital gains on the eligible assets and the double taxation is not eliminated in the foreign country, the foreign tax credits will be applicable in Japan by filing a request for correction assuming that the foreign income tax were paid in the year of departure.

(iv) Termination of grace period

- The amount of the exit tax liability should be paid at the end of the grace period.
- Interest tax corresponding to the grace period should also be paid.
- If the value of the eligible assets at the date of the termination falls below the value of the assets as of departure, the exit tax will be reduced by filing a request for correction.

(6) Timing of application

The above new rules discussed in 1 (Exit tax in the case of Departure from Japan) will be applied when eligible persons depart from Japan on or after 1 July 2015.

2. Exit Tax in the case of Gift, Inheritance or Bequest

In the case where the appreciated financial assets are transferred to a non resident individual by gift, inheritance or bequest, the exit tax will also be applied assuming the unrealized capital gains/losses on those assets were realized at the time that the gift, inheritance or bequest occurs.

This exit tax will be imposed when eligible persons' eligible assets are transferred to non resident individuals upon a gift, inheritance or bequest on or after 1 July 2015.

3. Special Measure for Foreign Exit Tax

When a resident individual who already paid a foreign exit tax on their eligible assets sells the eligible assets, the double taxation on the eligible assets will be eliminated by increasing the acquisition cost of the eligible assets for Japanese tax purposes to the value that was subject to the foreign exit tax.

This special measure for foreign exit tax will be applicable when events equivalent to events subject to exit tax in Japan occur in foreign countries on or after 1 July 2015.

4. Statute of Limitation

The statute of limitations for reassessment/determination of individual income tax by the tax office is 5 years in principle. When the exit tax regime (discussed in 1. and 2. above) is applied (excluding certain cases, e.g. where both a tax agent and a tax representative are appointed), the statute of limitations will be extended to 7 years.

This amendment will become effective on 1 July 2015.

II. AMENDMENTS TO REPORTING REQUIREMENT OF ASSETS/LIABILITIES

Before the 2015 tax reform, if an individual has an obligation to lodge their income tax return and their total income exceeds JPY20 million for a calendar year, the individual had to submit a ‘Statement of Assets/Liabilities’ together with their income tax return to declare the type, number and value of assets and amount of liabilities as of the end of the calendar year.

In order to ensure appropriate declaration of income and assets as a consequence of the introduction of the exit tax regime, the following amendments to the ‘Statement of Assets/Liabilities’ were made under the 2015 tax reform.

1. Amendments to Criteria for Submission and Items to be Declared

The criteria for submission of the ‘Statement of Assets/Liabilities’ was amended as followed:

Before amendment	Total income exceeds JPY20 million for a calendar year
After amendment	When meeting the following two criteria: (i) Total income exceeds JPY20 million for a calendar year; and (ii) Total value of assets as of the end of a calendar year is JPY300 million or more or Total value of the eligible assets for exit tax as of the end of a calendar year is JPY100 million or more

Information on each asset to be declared in the ‘Statement of Assets/Liabilities’ will be increased similarly to those to be declared in the ‘Statement of Overseas Assets’, which is to be submitted by permanent residents of Japan who own overseas assets valued at over JPY50 million as of the end of a calendar year.

For instance, location of the assets/liabilities, name/acquisition cost of securities will be additionally required to be declared in the new ‘Statement of Assets/Liabilities.’ Note that the acquisition cost of securities was newly added to items to be declared in the ‘Statement of Overseas Assets’ under the 2015 tax reform.

The value of assets should be assessed at ‘fair market value’ or ‘estimated value’ as of the end of the calendar year.

These amendments will be applicable to ‘Statement of Assets/Liabilities’ to be submitted on or after 1 January 2016.

[New format for ‘Statement of Assets/Liabilities’]

Statement of Assets/Liabilities as of 31 December XXXX						
Person having assets/liabilities		Place of domicile or residence				
		Name				
		Personal number				
Category	Type	Purpose of use	Place	Number	Value of assets/ Amount of liabilities	Other
•	•	•	•	•	•	
•	•	•	•	•	•	
•	•	•	•	•	•	
Total value of assets			Total amount of liabilities			

(The acquisition cost of assets should be stated in the column of 'Value of assets/Amount of liabilities' together with the value of assets.)

2. Special Measures for Additional Taxes

When a taxpayer understates the tax basis in the tax returns or fails to lodge tax returns by the due date, if a Correction (lodging an amended tax return or a tax return after the due date by the taxpayer, or taking action for reassessment/determination by the tax office) is made, additional tax for understatement or additional tax for failure to lodge will generally be imposed on the tax amount to be paid based on the Correction at the following rates:

Additional tax	Tax amount to be paid based on the Correction	Rate
Additional tax for understatement	Tax amount exceeding JPY500,000 or the tax amount declared in the original tax return, whichever is larger	15%
	Tax amount other than the above	10%
Additional tax for failure to lodge	Tax amount exceeding JPY500,000	20%
	Tax amount other than the above	15%

With respect to such additional taxes, the following special measures which are the same as those for 'Statement of Overseas Assets' were introduced to encourage people to accurately declare their assets/liabilities:

	Measure to <u>reduce</u> additional tax	Measure to <u>increase</u> additional tax
Cases where the special measures are applied	<ul style="list-style-type: none"> Where the Correction was derived from assets/liabilities declared in 'Statement of Assets/Liabilities' submitted by the due date 	<ul style="list-style-type: none"> Where 'Statement of Assets/Liabilities' was not submitted by the due date, or Where the Correction was derived from assets/liabilities not declared in 'Statement of Assets/Liabilities' submitted by the due date (including a case where the declaration was not sufficient)
Taxes subject to the special measures	<ul style="list-style-type: none"> Income tax on income derived from assets/liabilities Inheritance tax on assets 	<ul style="list-style-type: none"> Income tax on income derived from assets/liabilities
Measures	Rate of additional tax for understatement/additional tax for failure to lodge is reduced by 5%.	Rate of additional tax for understatement/additional tax for failure to lodge is increased by 5%.

Even when the 'Statement of Assets/Liabilities' is submitted after the due date, if it is made voluntarily (i.e. not because of anticipating that a reassessment or determination will be made due to a tax examination of assets/liabilities), such statement will be treated as being submitted within the due date for the purpose of the special measures.

The above special measures will be applied to income/inheritance taxes with respect to assets/liabilities to be declared in 'Statement of Assets/Liabilities' submitted on or after 1 January 2016.

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