
GMS Flash Alert

**Global Compensation Edition**

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# Japan - Tax Reform Includes Stock Option Taxation Changes for Start-Ups

Under Japan's 2023 tax reform proposals,[1] one of the requirements (the "exercise period requirement") for a stock option to be considered a "qualified stock option" will be relaxed in the case of stock options issued by certain unlisted Japanese "start-up companies" to their employees/directors.

## WHY THIS MATTERS

The relaxing of this requirement should provide an incentive for start-ups. The period during which individuals awarded such stock options can choose to exercise them and "defer" their taxability is extended (as noted below) to within 15 years after the right is granted, rather than as has been the case, the current maximum period of 10 years.

Extending the tax-preferential period for stock options means that they could be a more attractive way of compensating individuals in the start-up sector and give that sector a boost.

## Background

Under current stock options rules, there are several requirements that stock options granted by a company to its employees/directors (including those of a subsidiary) must meet in order to be treated as "qualified stock options." Treatment as a tax qualified stock option allows income from the exercise of such qualified stock options to be treated as taxable capital gain and deferred until the shares obtained from the qualified stock option exercise are sold, instead of being treated as employment income taxed at the time of the stock option exercise.

## Changes under 2023 Tax Reform

Under the 2023 tax reform proposals, the “exercise period requirement” will be relaxed in the case of stock options issued by certain unlisted Japanese “start-up companies” to their employees/directors (including those of a subsidiary) as described below.

| | Exercise Period Requirement for Certain Start-up Companies |
|---|---|
| Current Law | Option must be exercised after two years but before 10 years from the resolution date of the option grant. |
| Proposed Law | Option must be exercised after two years but before 15 years from the resolution date of the option grant. |

A “start-up company” is a Japanese company (“Kabushiki-Kaisha”) that has been in existence for less than five years, is unlisted, and meets certain other requirements.

## KPMG INSIGHTS

This measure – amongst others in the 2023 tax reform – is part of Prime Minister Fumio Kishida’s intention to support start-ups and entrepreneurial activity in Japan as integral to his government’s “new capitalism” agenda.

For start-ups that depend on the efforts of their employees to perform research and development, negotiate supply chains, and build relationships with manufacturers, the time to bring a product or service to market, while continuing to retain employees to keep the concern going, up to and beyond the time it has a sellable product or service, can be lengthy. So, this extension of the exercise period requirement will give them some “breathing room” to achieve their goals.

If employers have questions regarding existing rules, and/or the changes that apply to start-ups, what the conditions of eligibility are, and what the tax consequences are, they should contact their qualified global reward professional or a member of the Global Reward Services team with KPMG in Japan (see the below Contact Us section).

## FOOTNOTE:

1 For an English-language version of the key points of the FY 2023 tax reform on the website of Japan’s Ministry of Finance, click here. And in Japanese, see this webpage.

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### Contact us

For additional information or assistance, please contact your local GMS or People Services professional or one of the following professionals with the KPMG International member firm in Japan:

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