Guide to Japanese Taxes

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Japan Federation of Certified Public Tax Accountants’ Associations

* This material was compiled by the International Relations Committee of Japan Federation of CPTAs’ Associations based on the brochure, “Guide to Japanese Taxes and System of Certified Public Tax Accountants” issued by the Tokyo CPTAs’ Association.
* The information included in this material is based on the tax system effective as of 31 March 2011.

1. Organization of Tax Administration

The tax administration in Japan is classified into two categories depending on the right of taxation of national tax and local tax. The national government and the local governments administer various taxes as described below.

(1) Structure of National Tax Administration

Under the National Tax Agency, which is an external organ of the Ministry of Finance, there are 11 Regional Taxation Bureaus and the Okinawa Regional Taxation Office, under which 524 tax offices are placed to execute tax administration. Taxpayers must file returns and pay national taxes such as income tax, corporation tax and consumption tax to the tax office with jurisdiction over the location where the taxpayers reside.

(2) Structure of Local Tax Administration

Local taxes are administered by the Local Tax Bureau, an internal organ of the Ministry of Public Management, Home Affairs, Posts and Telecommunications, which is responsible for planning local taxes such as prefectural tax and municipal tax and for determining which governmental body has the right to levy taxes. The actual administration such as tax assessment and collection is executed by the local government that has the right of taxation. The prefectural tax offices and municipalities (cities, wards, towns and villages) are in charge of assessment and collection of prefectural taxes and municipal taxes respectively.

(3) Principle of “Taxation under law”

The Constitution of Japan provides in Article 30 that “The people shall be liable to taxation as provided by law” and in Article 84 that “No new taxes shall be imposed or existing ones modified except by law or under such conditions as the law may prescribe,” thereby declaring the state’s principle of “Taxation under law”. This clarifies the principle that since taxation is a means to transfer part of the people’s wealth to the state’s coffer to procure funds for public services, tax assessment and collection must be conducted on the basis of law.

(4) Self Assessment System

① Methods for establishing tax obligation

For establishing tax obligation, there are three methods which include “Self Assessment” method, “Official Assessment” method and the method to establish tax obligation at the time of assessment.

The self assessment method is the way to determine the tax amount to be paid on the basis of returns filed by taxpayers, and it is applied to most of major tax items in Japan, such as individual income tax, corporation tax, inheritance tax, gift tax, corporate inhabitant tax, enterprise tax and consumption tax.

The official assessment method is to determine the tax amount to be paid by tax administration offices, and it is applied to such tax items as property tax, automobile tax and additions to national tax.

In case of such taxes as withholding income tax and stamp tax, the tax amount to be paid is determined, without assessment procedures, simultaneously upon establishment of tax obligation.

As described above, taxation in Japan is based on the self assessment system.

This is the system in which taxpayers compute their tax amount, file tax returns and pay the tax voluntarily, and may be called the embodiment in taxation of the ideal of the Japanese constitution that calls for the principle of popular sovereignty.

② Filing tax returns and request for correction

There are following three types in filing tax returns.

a. Filing returns within the due date

Taxpayers paying tax under the self assessment system must file tax returns by the legally set deadline. Those returns filed according to this regulation are called tax returns filed within the due date.

b. Filing returns after the due date

Those who have failed to file returns within the due date may file returns even after the deadline, if the decision by the district director of the tax office has not yet been made.

c. Filing amended returns

Those who have already filed returns and those who have received decisions on correction may file amended returns, before corrections by the district director of the tax office, if they find the tax amount shown in their original returns understated.

Those who have filed returns in excessive tax amount may request correction of their tax amount to the district director of the tax office within their jurisdiction no later than one year from the original legal due date.

③ Blue return system

An individual or corporate taxpayer, with the approval of the tax office may file a blue return. Some tax privileges are granted to the blue return taxpayers.

This system is offered to encourage the spread of the self assessment system and promote practice of keeping proper books of account and records.

④ e-filing

Taxpayers can choose to use electronic filing or e-filing, also known as e-Tax and eLTAX, to file returns, pay tax, make applications or notifications.

(5) Tax Examination and Remedy System

① Tax examination and corrections/decisions

Under the self assessment system, a taxpayer’s tax obligation is established, in principle based on the returns filed by the taxpayer. However, when the filed returns are recognized to contain errors or irregularities, tax examinations will be conducted by the head of the tax office and tax amount will be determined based on the examination.

When the head of the tax office recognized it necessary, the taxpayer's account books and relevant records may be inspected, in accordance with the provisions of the law.

For those who have not filed tax returns, the head of the tax office will make the decision of tax liabilities, if it is found that they are liable to pay tax.

For those who have filed returns, the head of the tax office will make corrections on the tax amount when the results of examinations show that the tax amount on their respective tax returns is under-declared.

In case that tax is imposed additionally or newly as a result of correction or decision, prescribed additional tax (surcharge) will be imposed as penalty.

② Administrative protest system and judicial action

If a taxpayer is dissatisfied with the correction or decision by the head of the tax office, a protest may be filed with the head of the tax office.

If the taxpayer is not satisfied with the decision made on the protest, the taxpayer can file a request for reconsideration with the National Tax Tribunal.

Furthermore, if the taxpayer is not satisfied with the decision made by the National Tax Tribunal, he or she can file the case before the judicial court.

2. Major Taxes in Japan

	National Taxes	Local Taxes	
		Prefectural Tax	Municipal Tax
Taxes on profit and income	Income Tax Corporation Tax	Prefectural Inhabitants Tax Enterprise Tax	Municipal Inhabitants Tax
Taxes on gifts and inheritance	Gift Tax Inheritance Tax		
Taxes on properties		Automobile Tax	Property Tax Special Landholding Tax City Planning Tax Light motor Vehicle Tax Enterprise Establishment Tax
Taxes on consumption	Consumption Tax	Golf Course Utilization Tax	
Taxes on transactions	Stamp Tax Registration and License Tax	Real Property Acquisition Tax Automobile Acquisition Tax	

3. Taxes on Income

(1) Taxes on Individual Income

Income tax and inhabitants tax are levied on an individual's income – and enterprise tax levied to a certain degree.

① Income Tax

a. Income means total amount of revenue minus necessary expenses to earn that revenue during the year. Income is categorized tion10 types- interest, dividend, real estate, business, salary, retirement, forest land, transfer, temporary, and miscellaneous.

Individuals who have taxable income must compute their income earned between January and December every year and their tax liability (amount), and pay the tax under the self-assessed taxation system. However, salary earners are not required to file tax returns because their employers withhold tax from employees' wages and make the yearend adjustments.

Those required to file final returns are:

- those whose annual income from one source exceeds ¥20 million,
- those whose income from secondary sources, other than salary and retirement income exceeds ¥200,000,
- those who earn salaries from two or more sources

The period for filing final returns for income earned during the year is from February 16 to March 15 of the following year.

b. Classification of taxpayers

Taxes are levied on individuals according to their residential status. Residential status is classified into the following categories.

- Individuals
  - Residents*
    - Non-permanent residents**
    - Permanent residents***
  - Non-residents****

Notes: * Those who have an address (domicile) in Japan and have resided continuously in Japan for one year or more are regarded as residents.
Those who enter Japan as salary earners with the intention to reside in Japan are presumed to be residents immediately after their entry into Japan, unless it is clearly recognized that their stay in Japan will not be more than one year.

** Those that are not Japanese nationals and who have had an address (domicile) or residence in Japan continuously for not more than five years in the past ten years are regarded as non-permanent residents.

*** All residents other than non-permanent residents are permanent residents.

**** All individuals who are not residents are nonresidents.

c. Scope of taxable income

Classification		Scope of Taxable Income			
		Income from sources in Japan		Income from sources abroad	
		Paid in Japan	Paid abroad	Paid in Japan	Paid abroad
Resident	Non-permanent Resident	All income taxable	All income taxable	All income taxable	The income deemed remitted to Japan is taxable. (The income retained abroad is not taxable.)
	Permanent Resident	All income taxable	All income taxable	All income taxable	All income taxable
Non-resident		Income is taxable in principle		Income is not taxable	

d. Tax rate of income tax

Brackets of taxable income (Unit:¥1,000)		Tax rate (%)
Over	But not over	
—	1,950	5
1,950	3,300	10
3,300	6,950	20
6,950	9,000	23
9,000	18,000	33
18,000		40

② Inhabitants Tax

Prefectural inhabitants tax and municipal inhabitants tax are collectively called inhabitants tax. Such inhabitants taxes are levied on a per-capita basis and per-income basis for those who have an address (domicile) as of January 1, and inhabitants taxes on a per-capita basis on those who have an office or a house even if they do not live there.

The amount of inhabitant tax is calculated on the basis of income earned in the previous year. The tax rate of per income levy is 10% regardless of amount of income. The standard amount of per capita levy in a year is ¥4,000 regardless of amount of income.

(2) Taxes on Corporate Income

Taxes levied on corporate income in Japan include corporation tax as a national tax and corporate inhabitant tax and enterprise tax as local taxes.

① Corporation Tax

a. Corporation tax is levied on corporations' income. Corporations are divided into two categories: domestic corporations and foreign corporations. Domestic corporations have their head offices in Japan, while all corporations that are not domestic corporations are classified as foreign corporations. When a foreign corporation establishes a subsidiary or an affiliate company in Japan, those subsidiary or affiliate company is regarded as a domestic corporation. However, a branch office or a manufacturing plant set up in Japan by the foreign corporation is regarded as a foreign corporation.

b. Classification of taxpayers
Domestic corporations are liable to corporate tax both on Japanese source income and foreign source income. However, foreign corporations are subject to corporate tax only on specified Japanese source income.

c. Scope of taxable income
Domestic corporations are levied corporation tax on income for each of their business years and on income at liquidation. However, foreign corporations are subject to corporation tax only on income coming from sources in Japan during their business year.

d. Business year
Business year is the term to serve as the unit to calculate profit and loss of a corporation and is stipulated by the company's articles of incorporation.

e. Tax rates
Tax rate of 30 % is applied, but to an annual income of ¥8 million or less of a corporation capitalized at ¥100 million or less, a lower rate of 18 % is applied.

f. Final tax return
Corporations are required to file final returns within two months from the last day of their business year.

g. Place of tax payment
The place of tax payment for domestic corporations is the location of their head offices, and for foreign corporations, the location of their main permanent establishment in Japan, such as the main office.

h. Transfer price taxation
When the payment a corporation receives in a business deal with a partner abroad is less than arms' length price, or the payment the corporation makes in a similar deal exceeds arms' length price, that business deal with overseas partner is regarded as having been made at arms' length price.

i. Consolidated taxation system

The consolidated taxation system was introduced in Japan on April 2002. Under this scheme, a parent company and its subsidiaries are deemed to be a consolidated group which is subject to corporation tax. The scope of applicable corporations is a group of Japanese companies in which a Japanese parent company owns 100% ownership of other Japanese companies (subsidiaries). The parent company shall file the consolidated tax return based on aggregated taxable income.

j. Taxation system for corporate reorganizations

If a corporation reorganized its assets by means of merger, corporate division, investment-in-kind or share transfer, and the reorganization corresponded to certain requirements, the special tax treatment is applied and the recognition of the gains and losses on the transfer of the assets will be deferred.

k. Taxation system for 100% group

The taxation system for 100% group was introduced on October 2010. Under this scheme, a group of companies one of whom owns 100% of shares of other companies is deemed as one corporation for taxation purpose, and taxation on transfers of real estates or shares within the group will be deferred until the assets are sold outside of the group.

l. Taxation system for thin capitalization

Under the taxation system for thins capitalization, interest is partly excluded from a corporation’s deductible expenses when the corporation has borrowed money exceeding three times the amount of its capital from its foreign leading shareholders.

② Corporate inhabitants tax

This tax is levied by the prefecture and municipalities (city, town or village) where a corporation has business establishments.

③ Enterprise tax

This is one of the prefectural taxes imposed on businesses corporations operating in the prefecture.

(3) Withholding Income Tax

When corporations make payment of more than a certain amount to individuals or corporations, they must withhold income tax from the amount paid and pay the withheld tax to the tax office of its jurisdiction. The scope of income subject to tax withholding and withholding rates differ, depending on whether the payee is a resident (including domestic corporations) or a nonresident (including foreign corporations). A residents’ income subject to withholding tax include interest, dividend, salary, retirement allowance, and remuneration. Incomes from retirement benefits and salary are subject to progressive tax rates, while a tax rate of a maximum of 20 percent is applied to the other types of incomes.

Income tax for nonresidents can be classified as follows.

Outlines of Income Tax for Nonresidents

<table>
<tr><th rowspan="2">Types of Nonresidents
Types of income</th><th colspan="3">Those who have a permanent establishment in Japan</th><th rowspan="2">Those who do not have a permanent establishment in Japan</th><th rowspan="2">Withholding tax</th></tr>
<tr><th>Those who have branch office or other fixed establishment for business (No.1PE)</th><th colspan="2">Those who have been operating construction work, etc. for over one year, or have agent(s), etc. who has certain qualifications (No.2PE, No.3PE)</th></tr>
<tr><td>Income from business</td><td colspan="3" rowspan="3">Total taxation</td><td>Exempted</td><td>None</td></tr>
<tr><td>Income from assets</td><td rowspan="2">Total taxation</td><td>None</td></tr>
<tr><td>Other income from sources in Japan</td><td>None</td></tr>
<tr><td>Distribution of profits from association contract business</td><td colspan="3" rowspan="4">Total taxation after levying withholding tax</td><td>Exempted</td><td>20%</td></tr>
<tr><td>Counter-values for land transfers, etc.</td><td rowspan="3">Total taxation after levying withholding tax</td><td>10%</td></tr>
<tr><td>Counter-values for business rendering human services</td><td>20%</td></tr>
<tr><td>Rental and other revenues from leasing real estate</td><td>20%</td></tr>
<tr><td>Interest, etc.</td><td rowspan="9">Total taxation after levying withholding tax</td><td rowspan="9">Subject to business in Japan</td><td rowspan="9">Subject to business outside of Japan</td><td rowspan="9">Separate taxation at source</td><td>15%</td></tr>
<tr><td>Dividends, etc.</td><td>20%</td></tr>
<tr><td>Interest on loans</td><td>20%</td></tr>
<tr><td>Rents and other usage fees</td><td>20%</td></tr>
<tr><td>Salaries, other counter-values for rendering human services, public pensions, retirement allowances, etc.</td><td>20%</td></tr>
<tr><td>Prize money for advertisement of business</td><td>20%</td></tr>
<tr><td>Pensions and others based on contracts of life insurance</td><td>20%</td></tr>
<tr><td>Compensation benefits from installment savings</td><td>15%</td></tr>
<tr><td>Distribution of profits based on anonymous association contracts, etc.</td><td>20%</td></tr>
</table>

Japan currently has tax treaties with 59 countries, and under those tax treaties, there could be reductions in tax rates or tax exemptions. In order to receive application of these tax relief measures, those who receive tax payment are required to submit notification concerning the tax treaties to the relevant tax office through those who are paying the tax.

4. Taxes on Gifts and Inheritances

(1) Gift Tax

Those who acquired property by gift during a year must file a return the following year and pay gift tax. The return must be filed during the period from February 1 to March 15 of the following year.

Those who received gifts after January 1, 2003, can opt for tax settlement at the time of inheritance under certain conditions. The taxable value is the amount after deducting the basic allowance (¥1,100,000) and the spouse allowance (¥20,000,000).

<Taxable amount and tax rate>

Taxable amount (Unite:¥1,000)		Tax rate
Over	But not over	%
—	2,000	10
2,000	3,000	15
3,000	4,000	20
4,000	6,000	30
6,000	10,000	40
10,000		50

(2) Inheritance Tax

Those who acquired property by inheritance or bequest must file a return and pay inheritance tax, in principle, within ten months after the date of inheritance. The person who died is called ancestor and the person who inherited property is called inheritor.

Scope of property subject to inheritance tax varies depending on whether the inheritor's address (domicile) is in Japan or outside Japan.

<Taxable amount and tax rate>

Taxable amount (Unit:¥1,000)		Tax rate
Over	But not over	%
—	10,000	10
10,000	30,000	15
30,000	50,000	20
50,000	100,000	30
100,000	300,000	40
300,000		50

5. Tax on Consumption

Consumption tax is levied on the sale and lease of goods and providing services in Japan and the business enterprises engaged in such business activities are obliged to pay consumption tax. However, because consumption tax is added on to the prices of goods and services, the tax is ultimately borne by consumers. Imported goods are taxable, but export products are exempted from taxation.

Individuals and corporations who collect consumption tax in their business transactions must file returns on the amount of consumption tax to be paid - the net amount of consumption tax received minus that paid by economic transactions during the accounting period.

The tax rate is 5% including 1% of local consumption tax.

6. Taxes on Properties and Transactions

(1) Property Tax and City Planning Tax

① Fixed property tax

Individuals and corporations who own real property, such as land and houses, and any depreciable assets for business, such as machines and equipment must pay fixed property tax to the municipality.

The annual tax rate is 1.4%. The municipal governments are allowed to apply higher rate than 1.4% but not allowed to exceed 2.1%.

② City planning tax

Those who own real property such as land and houses must pay this tax to the municipality. This tax is aimed at financing city planning and land readjustment projects.

The tax rate is 0.3% of the value of the land and buildings.

(2) Automobile Tax and Light Motor Vehicle Tax

① Automobile tax

Car owners must pay this tax to the prefecture on the location where their automobiles are regularly garaged or stored.

② Light motor vehicle tax

Owners of motorized bicycles, light motor vehicles, small-sized special motor vehicles and two-wheeled small-sized motor vehicles must pay this tax to the municipality on the location where their vehicles are regularly garaged or stored.

(3) Enterprise Establishment Tax

Corporations and individuals who do business in big cities with population of 3 millions or more must pay this tax in accordance with the size of the floor space of their business establishment and with the total amount of salaries paid to the employees.

(4) Registration and License Tax

① Real property registration tax

Corporations and individuals who have registered the ownership’s right of land or a building must pay this tax.

② Commerce registration tax

This tax must be paid at the time of establishment of a company, capital increase, registration of a branch, changes in board directors, change in corporate name, and other commercial registrations. This tax must be paid also when patents, copyrights and qualifications are registered.

(5) Real Property Acquisition Tax

Corporations and individuals who have acquired land or a building must pay this tax to their prefecture.

(6) Stamp Tax

Corporations and individuals who have prepared certificates of economic transactions such as various contracts, securities, receipts, etc. must pay stamp tax to the government.