

# Japan: Inbound Tax Alert

## Japan Tax Convention Update

November 2016, No. 17

### In Brief

Japan has been active in negotiating tax treaties in the latter half of 2016 and has recently concluded amendments to its convention with Belgium and a newly signed agreement with Slovenia. In addition, a revised treaty signed with Germany and a protocol to the existing Japan-India treaty both entered into force this October. Japan has also agreed in principle on a new convention with Austria, and is engaged in active negotiations with Kenya and Kyrgyzstan. Japan's new bilateral tax conventions show a similar pattern of reduced withholding tax rates to encourage cross-border investment, strengthened anti-avoidance measures in-line with the OECD BEPS initiative, and recognition of internal dealings between a corporation's head office and its permanent establishment (PE) using the arms-length principle in accordance with the Authorized OECD Approach (AOA) to attribution of income.

### Summary of Recently Negotiated Tax Conventions

Below is a summary of Japan's recently signed tax treaties with some of the key updates included:

	Withholding Tax (WHT)					Other	
	Dividends		Interest		Royalties	Internal Dealings w/ PE (AOA)	Anti-Avoidance Measures
	Companies with certain ownership (minimum %)	Other	Qualified <sup>1</sup>	Other			
<b>Belgium / Japan Tax Convention</b>							
Existing	<ul style="list-style-type: none"> <li>■ 5% (25%, paid by Belgium Co.)</li> <li>■ 10% (25%, paid by Japan Co.)</li> </ul>	15%	10%		10%	N/A	N/A
Amended	0% (10%)	10%	0%	10%	0%	Recognized	<ul style="list-style-type: none"> <li>■ LOB<sup>2</sup></li> <li>■ PPT<sup>3</sup></li> </ul>
<b>Germany / Japan Tax Convention</b>							
Former	10% (25%, for 12 mo. paid by Japan Co.)	15%	0%	10%	10%	N/A	N/A
Amended	<ul style="list-style-type: none"> <li>■ 0% (25%, for 18 mo.)</li> <li>■ 5% (10%, for 6 mo.)</li> </ul>	15%	0%		0%	Recognized	<ul style="list-style-type: none"> <li>■ LOB<sup>2</sup></li> <li>■ PPT<sup>3</sup></li> </ul>
<b>Slovenia / Japan Tax Convention</b>							
New	5%	0%	5%		5%	Recognized	PPT <sup>3</sup>

1. Qualified interest means with respect to Belgium interest paid and beneficially owned by enterprises, etc., with respect to Germany interest paid on government bonds, and with respect to Slovenia interest received by governments, etc.

2. "Limitation of Benefits" – treaty clause limiting benefits of convention to only residents who meet a series of objective criteria

3. "Principle Purpose Test" – clause denying benefits if one of the principle purposes of a transaction was to obtain treaty benefits

## Other Notable Provisions

In addition to reduced withholding tax rates, recognition of internal dealings with a PE, and anti-avoidance measures, Japan's newly signed tax treaties and protocols contain some of the following additional provisions:

### Belgium

#### 1) Mutual Agreement Procedure

The new treaty includes a mandatory arbitration provision for mutual agreement procedure cases that the competent authorities are unable to resolve within two years.

#### 2) Assistance in Collection of Tax Claims

A new provision in the treaty requires the mutual assistance in collection of tax claims between the two countries.

### Germany

#### 1) Taxing Rights on Capital Gains

A new clause in Article 13 gives taxing rights to a Contracting State on capital gains arising from the alienation of shares deriving at least 50% of their value from immovable property located in that Contracting State.

#### 2) Elimination of Double Taxation

A new provision allows German residents to avoid double taxation by generally exempting income taxed in Japan from German taxation, while Japan residents are allowed a credit against taxable income arising in Germany.

#### 3) Mutual Agreement Procedure

The new treaty includes a mandatory arbitration provision for mutual agreement procedure cases that the competent authorities are unable to resolve within two years.

### India

#### 1) Exchange of Information

The recently signed protocol includes a provision for the exchange of information between tax authorities for the purposes of carrying out the convention.

#### 2) Assistance in Collection of Tax Claims

A new provision included in the protocol requires the mutual assistance in collection of tax claims between the two countries.

## Effective Dates

The effective dates for Japan's newly signed tax treaties are as follows:

	Belgium <sup>1</sup>	Germany	Slovenia <sup>1</sup>
Enter into force	30 <sup>th</sup> day after countries exchange notification of ratification	28 October 2 016	30 <sup>th</sup> day after countries exchange notification of ratification
WHT	On payments made on or after 1 January 2018	On payments made on or after 1 January 2017	On payments made on or after 1 January 2018
Other taxes	For amounts taxable on or after 1 January 2018	For amounts taxable on or after 1 January 2017	For amounts taxable on or after 1 January 2018

1. Dates listed in chart assume that treaty is ratified by both parties in 2017.

## Deloitte's View

Japan's recent efforts to update and expand its treaty network show consistency with a global shift in the tax landscape towards strengthening of measures to prevent tax avoidance, increased transparency between tax authorities, and the arm's length attribution of income in accordance with transfer pricing principles.

Such efforts are in-line with the aims of the OECD BEPS initiatives on anti-avoidance and transparency, as well as Japan's commitment to the adoption of the AOA approach to attribution of income. Japan is considered a first-mover in regards to both in the Asia-Pacific region.

A reduction in withholding tax rates on dividends, interest, and royalties, as well as clauses that aim to prevent double taxation, are both welcome signs for cross-border investment into and out of Japan.

However, given the proliferation of anti-avoidance measures in Japan's recent treaties, it is important that foreign investors ensure that there are sound business reasons for the way in which they structure their transactions with Japan, and that their entities which seek to benefit from a bilateral treaty with Japan have genuine substance.

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## Contacts

### Inbound Group, Deloitte Tohmatsu Tax Co.

Not all articles or facts and circumstances are covered in this alert. If you have any questions regarding your specific situation, please contact one of the tax professionals at our Deloitte office in Tokyo as follows:

Yang Ho Kim, Inbound Group Leader      [yangho.kim@tohmatu.co.jp](mailto:yangho.kim@tohmatu.co.jp)      +81 3 6213 3841

### Business Tax Services

Sunie Oue, Partner      [sunie.oue@tohmatu.co.jp](mailto:sunie.oue@tohmatu.co.jp)      +81 3 6213 3753

Jun Takahara, Partner      [jun.takahara@tohmatu.co.jp](mailto:jun.takahara@tohmatu.co.jp)      +81 3 6213 3946

### Indirect Tax Services

Chikara Okada, Partner      [chikara.okada@tohmatu.co.jp](mailto:chikara.okada@tohmatu.co.jp)      +81 3 6213 3900

### Global Employer Services

Russell Bird, Partner      [russell.bird@tohmatu.co.jp](mailto:russell.bird@tohmatu.co.jp)      +81 3 6213 3979

### Transfer Pricing

Timothy O'Brien, Partner      [timothy.obrien@tohmatu.co.jp](mailto:timothy.obrien@tohmatu.co.jp)      +81 3 6213 3923

Jun Sawada, Partner      [jun.sawada@tohmatu.co.jp](mailto:jun.sawada@tohmatu.co.jp)      +81 3 6213 3927

## Issued by

### Deloitte Tohmatsu Tax Co.

#### Tokyo Office

Shin-Tokyo Building 5F, 3-3-1 Marunouchi, Chiyoda-ku, Tokyo 100-8305, Japan

Tel: +81 3 6213 3800

email: [tax.cs@tohmatu.co.jp](mailto:tax.cs@tohmatu.co.jp)

Corporate Info: [www.deloitte.com/jp/en/tax](http://www.deloitte.com/jp/en/tax)

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