

# Japan: Inbound Tax Alert

## Inheritance and gift tax

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### Overview

Japan has an inheritance and gift tax system in which the obligation to settle the tax is upon the recipient of the property rather than on the giver or estate of the deceased. For inheritance tax, under the Japanese Civil Code, the heirs are determined to have received their inheritance from the time of death of the individual, even when the actual distribution of property does not take place until sometime later. The obligation to file an inheritance tax return and pay the taxes lies with the heir and legatees, not the administrator of the estate.

Historically there has been no concept of non-permanent resident or permanent resident as is found for individual income tax purposes, and instead the taxpayer types are categorized based on the domicile of the heir / recipient and the deceased / giver.

### Domicile for purposes of inheritance and gift tax

A domicile generally is defined as the base of one's living, which is determined based on the objective facts (a person generally cannot have more than one domicile). Facts that may play a role in determining whether a domicile exists for these purposes include: (1) whether permanent residency has been granted, (2) whether the person is residing in Japan, (3) the presence of family in Japan, (4) the presence of property in Japan, (5) employment in Japan, etc. Therefore a foreign national residing in Japan or being employed in Japan for even a short period of time could inadvertently create a domicile and subject their heirs to the tax if a bequest or gift is made.

In order to determine the extent they are subject to Japanese inheritance / gift taxes, a recipient of property needs to determine what category of taxpayer they are.

### Pre-1 April 2017 law

Historically, the scope of inheritance tax has been dependent on the nationality of the heirs / donees and domicile of both the heirs / donees and decedent / donor.

Individuals who received an inheritance or gift whilst domiciled in Japan would be subject to Japanese inheritance and gift tax regardless of the location of the assets. Similarly, where an individual domiciled in Japan passed away / made a gift, their heirs / donees would be subject to Japanese inheritance and gift tax on Japan located assets. It was considered that this system, which extended to foreign nationals temporarily in Japan, acted as a disincentive to attracting foreign nationals to work in the country.

### 2017 Tax Reforms – With effect from 1 April 2017

In the 2017 Tax Reforms, the government has introduced a new category of taxpayer for the purposes of inheritance and gift tax. Foreign nationals considered temporarily living in Japan are subject to inheritance and gift tax only on Japan located assets provided the exchange happens with another temporary resident of Japan or an overseas foreign resident. A foreign national will be considered living temporarily if they are in Japan less than 10 out of the last 15 tax years and living under a category of visa covered under Table 1 of the Immigration Control and Refugee Recognition Act (which includes work related visas).

Another change following the reforms affects individuals leaving Japan. Whereas previously, individuals who were Japanese nationals and domiciled in Japan within the past 5 years would remain subject to Japanese inheritance and gift taxes on a worldwide basis even after losing their domicile in Japan, with effect from 1 April 2017, this look back period will be extended from 5 years to 10 years.

Furthermore, for the first time, foreign nationals who were domiciled in Japan and who leave will have a

trailing exposure to Japanese inheritance and gift taxes. From 1 April 2017, where the decedent / gift donor was domiciled in Japan in the last ten years, the recipient of the gift / inheritance will be subject to Japanese Gift and Inheritance tax on worldwide assets received. The exception is if the decedent / donor can be considered a Short Term Visitor (namely a foreign national who was domiciled in Japan for 10 years or less out of the last 15 years up to the date of inheritance). In practice, due to the 10 out of 15 year test, this would mean a long term foreign resident (i.e. more than 10 year resident) of Japan would have a potential exposure window of up to 5 years following their departure. Beyond which they would qualify as a Short Term Visitor.

Foreign nationals who left Japan prior to 1 April 2017, will not be subject to the lookback rules.

The following table reflects the new rules for inheritance and gift tax as of 1 April 2017.

Person from whom inheritance/ gift is received	Person Receiving the inheritance/ gift		Domicile in Japan (Regardless of nationality)	Foreigners temporarily living in Japan*	No domicile in Japan		
					Japanese nationality		No Japanese nationality
					Domicile in Japan within 10 years before death/ gift	No domicile in Japan within 10 years before death/ gift	
Domicile in Japan	Foreigners temporarily living in Japan*			Only assets in Japan taxable		Only assets in Japan taxable	
	No domicile in Japan	Domicile in Japan within 10 years before death/ gift	Individuals other than Short-term visitors				
Short-term visitors**				Only assets in Japan taxable		Only assets in Japan taxable	
No domicile in Japan within 10 years before death/ gift				Only assets in Japan taxable		Only assets in Japan taxable	

 Inheritance/ gift tax due on worldwide assets  
 Inheritance/ gift tax due on Japan assets

\* A foreign national who is considered temporarily living in Japan is one who is in Japan for 10 years or less out of the last 15 years and living under a category of visa covered under Table 1 of the Immigration Control and Refugee Recognition Act (which includes work related visas).

\*\* A short-term visitor is a non-Japanese national who was domiciled in Japan for 10 years or less out of the last 15 years up to the date of inheritance or gift.

### Deloitte's View

Recent changes to the inheritance tax rates and basic exemption law had increased the chance that a foreign national residing in Japan could be impacted by the Japanese Inheritance and Gift tax system and, contrary to the Government's intention to attract foreign business talent, was viewed by the foreign business community as a deterrent factor.

This new more relaxed regime is a welcome move as it has effectively removed most expatriates temporarily working in Japan from the scope of the inheritance and gift tax system. However, the fact that the look back rules have been extended to include longer term foreign residents of Japan, has created a new concern, particularly for longer term residents who had plans to leave the country and / or retire overseas.

The introduction of the new temporary resident status is also now the second recent tax change where the nature of an individual's visa has a direct bearing on their Japan tax exposure. The first being the new exit tax regime that was introduced in 2015 and which will first affect foreign nationals on non-work type visas from 2020. Companies may therefore wish to consider how to better identify cases where employees are considering applying to change their visa status so they can help their employees understand the tax consequences of doing so as well as how to mitigate any potential tax exposure that may arise as a result (for example by way of a life insurance policy, appropriate wording in transfer policies etc.).

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