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ICEbreakers: Unlocking Japan

Hot topics

2018 tax reform: The National Diet enacted the 2018 tax reform proposals on 28 March 2018, which include the following major corporate tax changes:

- The wage increase tax credit regime is expanded for companies that increase wages.
- Tax incentives for promoting information collaboration will be introduced from the effective date of the Productivity Improvement Act to 31 March 2021.
- The rules on corporate reorganizations are revised.
- The conditions for eligibility for certain R&D or other tax incentives are tightened.
- The definition of a permanent establishment (PE) will be expanded to align Japanese domestic tax law with the definition under the OECD's BEPS project for fiscal years beginning on or after 1 January 2019 for corporations and from calendar year 2019 for individuals.

Overview of some key items in the reform

- **Tax incentives for promoting information collaboration:**

  If a company obtains certification for its innovative data utilization plan and develops software according to that plan, assets acquired and used for information collaboration will be eligible for special depreciation (30% of the acquisition cost) or a credit (5%, or if certain conditions are not satisfied, 3%).
- **Tightening of R&D or other tax incentives:**

  If a large company does not satisfy any of the following for a fiscal year beginning from 1 April 2018 to 31 March 2021, certain tax credits will not be available to the company for that fiscal year. However, this will not apply to a fiscal year (excluding the fiscal year in which the company was established or merged) for which the company's profit is equal to or less than the profit for the previous fiscal year:
  - Average wage payments > Comparative average wage payments; or
  - Domestic capital investment > 10% of total depreciation Costs
- **Revision of PE related provisions:**
  - Revision of PE definition
    - Expansion of the scope of a dependent agent PE
    - Reduction of the scope of an independent agent
    - Limitation on activities excepted from PE recognition
  - Clarify rules when there are differences between tax treaties and Japanese law.
- **Other:**
  - Revisions related to corporate reorganizations
  - Amendments to the anti-tax haven rules (i.e. CFC rules)
  - Amendments to Japanese law for the implementation of the OECD Multilateral Instrument.

Revision of transfer pricing administrative guidelines

The National Tax Agency (NTA) released a revised version of the Commissioner's Directive on the Operation of Transfer Pricing on February 23, 2018, which include the following important changes:

- **Clarification on the relationship between tax audits and APAs:**
  - Even where a taxpayer requests a rollback in an APA application, a tax examiner is not barred from carrying out an audit for the rollback years.
  - When an APA is being discussed or agreed, tax filings (limited to those relating to transfer prices covered by the APA) will not be subject to tax audits for the APA years.
- **Intragroup services:**
  - Certain low value adding intragroup service transactions will be deemed to be at an arm's length if the service is priced on a cost-plus 5% basis.
  - The amended Administrative Guidelines provide comments on shareholder activities that would not be considered services to foreign related parties (and thus would not justify a charge to the foreign related parties).
- Note: the Administrative Guidelines do not have the force of law in Japan and are not binding on Japanese taxpayers, but they are an important source of guidance for how the Japanese authorities are likely to interpret transfer pricing rules in Japan.

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