Japan: 2013 tax reform proposal may impact globally mobile employees

February 1, 2013

In brief

The 2013 tax reform proposal submitted by the Cabinet Office Tax Commission known as *Taiko,* (the 2013 Tax Reform Proposal), was released on January 29, 2013 upon approval by the Cabinet. The proposed tax law changes will be submitted to the Diet this month for consideration.

This Global Watch focuses on the proposed income tax reforms and their impact on individual taxpayers in Japan. The 2013 Tax Reform Proposal includes, among many provisions, an additional national tax bracket of 45% for taxpayers with more than 40 million yen of taxable income (effective January 1, 2015). Another significant proposal is the introduction of non-taxable Individual Savings Accounts (coinciding with the reversion of the separate 10% tax rate on dividends and capital gains on listed stock to 20% at the beginning of 2014) and an increase in the home loan credit for homeowners.

In detail

Japan's top tax rate increases to approximately 56%

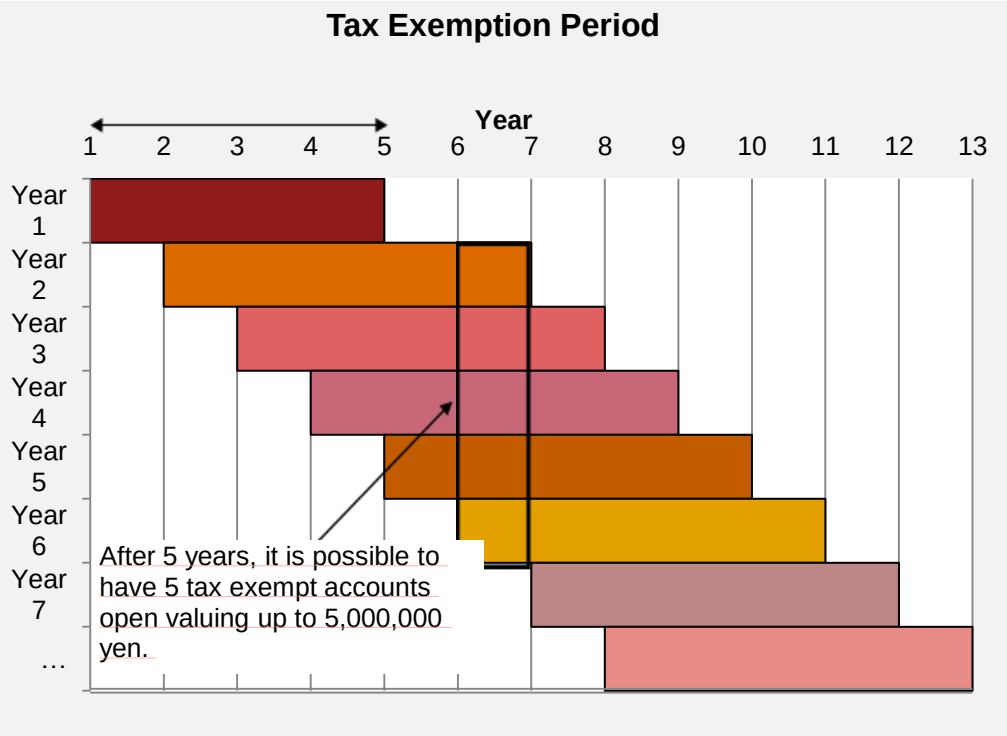
Currently, the top national tax bracket is 40% for taxpayers with taxable income of more than 18 million yen. Effective January 1, 2015, an additional national tax bracket of 45% for taxpayers with more than 40 million yen of taxable income will be added. When combined with the surtax of 2.1% that came into effect in 2013 and the local inhabitant's tax of 10%, Japan's top individual income tax rate will climb to nearly 56%.

Separate tax rates on capital gains and dividends

The temporary separate tax rate of 10% on capital gains and dividend income on listed stock will expire on December 31, 2013 and the government has indicated that it will not be extended unlike previous years. Beginning January 1, 2014, the separate tax rate on capital gains and dividend income will revert back to 20%.

Introduction of Individual Savings Accounts

Also, beginning January 1, 2014, the government will implement non-taxable accounts (also known as Individual Savings Accounts or ISAs) that were first introduced in the 2010 Tax Reform Proposal. The ISAs will operate from January 2014 to December 31, 2023 and individuals will be allowed to contribute up to 1 million yen of listed stock to each ISA. Individuals will be allowed to open one ISA per year and up to 5 ISAs in total (contributions of up to 5 million yen of listed stock). The earnings or gains from sales of listed stock in these accounts will not be taxed for up to 5 years. Please see the chart below.



Taxation of investment income

A significant proposed tax reform in the area of investment income involves the deductibility of capital losses. The proposed reform is that capital losses from unlisted securities (non-publicly traded securities) will not be deductible against capital gains income from listed securities. Net capital losses from unlisted securities cannot be carried forward so they will be unutilized.

Also, one of the major objectives of the 2013 Tax Reform Proposal is to align the taxation of income from bonds with income from stock. Starting January 1, 2016, income from bonds will be taxed separately and will be categorized into listed and unlisted. Also, capital gains from the sale of bonds is currently not taxable but similar to stock, they will become taxable. Capital losses from publicly traded bonds will also be deductible against dividend income from publicly traded stock, publicly traded bond interest and stock capital gains income. In addition, similar to listed stock, capital losses from publicly traded bonds will be carried forward for up to 3 years.

Increase in home loan credit

The government has proposed to increase the maximum allowable home loan credit from the current amount of 200,000 yen per year (for up to 10 years for a total of 2 million yen) to 400,000 yen per year (4 million yen in total) for houses purchased and occupied between April 1, 2014 and December 31, 2017. Also note that consumption taxes are scheduled to increase from 5% to 8% beginning on April 1, 2014 and then to 10% beginning on October 1, 2015.

For lower income taxpayers who cannot utilize the maximum credit for National tax purposes, a credit is allowed against their local inhabitants taxes. The maximum allowable credit for local inhabitants tax purposes will increase from a maximum of 97,500 yen per year to 136,500 yen per year. The sum of the national and local inhabitants tax credits cannot exceed 400,000 yen per year.

Offshore assets

Regarding the Offshore Assets Reporting Form, which is effective starting with the 2013 tax year, the Tax Commission is proposing a change to how a security will be determined to be offshore. The government will now use the location of where the security is held to determine whether it is an offshore asset (instead of the location of the issuing company of the security.) For instance, shares of a Japanese company held with an American brokerage company would be considered an offshore asset.

Changes to interest rates

Starting January 1, 2014, the interest rate charged on delinquent taxes and paid on tax refunds will decrease to

reflect the decrease in the general market rate.

Potential future changes

In the future, the government may further align the taxation of securities by taxing derivatives in the same way as income from bonds and stock. Regarding ISAs, the government is also contemplating expanding the type of investments that could be held in these accounts (expanding beyond just listed stock).

The takeaway

We recommend that globally mobile employees and their employers start thinking about the potential implications of the 2013 Tax Reform Proposal and how they may impact their businesses. For example, employers who tax equalize their higher income employees in Japan should plan for the potential increases in tax rates and the resulting cost increases to their mobility programs.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact the following representatives from PwC Japan Tax Tokyo:

Nasir Majid
+81 3 3539 6310
nasir.majid@jp.pwc.com

Marcus Wong
+81 3 3539 6406
marcus.wong@jp.pwc.com

Yuka Sakamitsu
+81 3 3539 6411
yuka.y.sakamitsu@jp.pwc.com