



# Financial Services Tax News

Financial Services Tax Group

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## Proposed 2008 Japanese Tax Reforms regarding an Independent Agent Exception

On December 13, 2007 the Liberal Democratic Party ("LDP"), the majority party in the Lower House of the Diet, released its proposal for tax reforms to be enacted from 1 April 2008.

A particular item of interest to the fund industry is a proposal that an independent agent exception be created to allow Japan-based investment managers to manage client funds without exposing the clients to Japanese taxation from such management. The proposed change is to amend Japanese domestic law and introduce an "independent agent exemption" to the dependent agent permanent establishment ("PE") rules. It is anticipated that this independent agent exemption may be broadly in line with OECD model treaty established precedents and is consistent with the Financial Service Agency's ("FSA") stated objective over the past several months of providing some type of tax relief for funds managed by Japan-based fund managers. No further details with regard to this proposal have been released.

Whilst the change applies generally, the proposal is very welcome news for Japan's fund industry. In particular, it may, for example, allow non-resident funds (and consequently their investors) to trade in Japan without creation of a PE, assuming the Japan based fund advisor/service provider meets the independent agent exception. Unlike other fund management centers (the UK, Singapore and Hong Kong, for example), which have been successful in attracting and nurturing advanced fund management centers, current Japanese tax rules do not have a safe harbor trading rule or otherwise allow non-resident funds to trade in Japan. Accordingly, fund managers to date have been required to restrict the range and scope of activities that could effectively be undertaken in Japan without unduly subjecting the offshore fund (and consequently its investors) to Japanese taxation.

At this point, the scope of the independent agent exemption has not yet been made clear. Thus, it is unclear both as to the types of investment managers that can qualify as "independent" and unclear as to the types of investments within its scope. The legislation is likely to take effect on or after April 1, 2008.

The LDP's proposal contains a number of other changes of interest to the financial services community. These will be described in our December News Alert to be released later this month.

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