

# Japan Tax Update

Monthly tax update



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PricewaterhouseCoopers Tax (Zeirishi-Hojin PricewaterhouseCoopers) is the largest professional tax corporation in Japan with more than 480 staff.

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The intention of this Japan Tax Update is to provide an outline of the Japanese tax reforms for 2007 based on the Reform Act that was promulgated on March 30, 2007.

We recommend that you consult with PricewaterhouseCoopers for specific advice and do not take any action based solely on the contents of this newsletter.

## Outline of 2007 Tax Reform

On March 30, 2007, the Tax Reform Act was promulgated and subsequently enacted on April 1, 2007. This issue exclusively deals with the 2007 tax reform.

### **1. Corporate Taxation**

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- (2) Directors remuneration
- (3) Amendments in relation to the application of revised accounting standards

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- (5) Deduction for contributions

## **10. Individual Tax**

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## 1. Corporate Taxation

### (1) Depreciation on fixed assets

#### 1) Abolishment of the final depreciable limit and residual value

The final depreciable limit and residual value for fixed assets will be abolished and the depreciation on fixed assets will be treated as follows:

- a) Fixed assets which are acquired on or after April 1, 2007 (including fixed assets acquired before April 1, 2007 but placed into the business on or after April 1, 2007) can claim depreciation until the depreciated balance is JPY 1 yen for each asset. For these assets, the rate applied for accelerated balance method will be 250% of the rates under the straight line method. When the depreciation expense under this accelerated method falls below the depreciation expense as calculated using the depreciation rate provided in the table of the Enforcement Order, the remaining balance is depreciated on a straight line basis over the remaining useful life of the asset with a residual value of 1 yen.
- b) Fixed assets which are acquired on or before March 31, 2007 will be depreciable using the old method. However, the 5% residual value under the old method will be depreciable on a straight line basis over five years starting from when the old depreciable limit was reached.

#### 2) Shortening of useful life for certain assets

The statutory useful life will be shortened with regard to the following three types of equipment:

The amended useful life is applicable for calculating the depreciation expense in the tax year starting on or after April 1, 2007.

- a) Flat-panel display manufacturing equipment: 5 years (previously 10 years);
- b) Film material manufacturing equipment for flat panel displays: 5 years (previously 10 years);  
and
- c) Photo resistant manufacturing equipment for semiconductors: 5 years (previously 8 years).

### (2) Directors remuneration

#### 1) Fixed monthly payments

Before the amendment, a corporation is allowed to claim a deduction for director compensation which is paid in the form of "fixed monthly payments" without any advance notice to the tax office provided that the relevant legal procedures have been followed (i.e., approval at a shareholders meeting or within the maximum amount specified in the corporation's by-laws). However, if the monthly amount is increased or decreased by way of resolution at a shareholders meeting or compensation committee, such revision should be made within three months from the beginning of the fiscal year. A decrease to fixed monthly payments may be made after three months from the beginning of the fiscal year if the corporation has a specific reason, i.e., a worsening of the financial condition of the corporation or a similar situation.

By the 2007 Tax Reform, a corporation is allowed to claim a deduction for fixed monthly payments where a revision of the amount of the payment (increase or decrease) is made as a result of a change in the position of the director.

#### 2) Fixed payments in accordance with an advance notice to the tax office

Before the amendment, a pre-determined bonus is deductible provided the corporation has filed an advance notice with the tax office by the earlier of (i) three months from the beginning of the accounting fiscal year or (ii) the date the relevant director commences the provision of his or her services.

By the 2007 Tax Reform, the relevant periods would be extended by one month, i.e., the earlier of (i) four months from the beginning of the accounting fiscal year or (ii) one month after the date of shareholders meeting in which directors remuneration is approved.

### 3) Directors' payment which does not require an advance notice to the tax office

If certain non-fixed payment(s) are made to a director which satisfy certain approval conditions (i.e., a pre-determined bonus), it is necessary to file an advance notice with the tax office so that these payments are deductible.

By the 2007 Tax Reform, such payment(s) will be deductible without advance notice if the corporation making the payments is not a family corporation as defined the corporate tax law.

The above amendments are applicable to the tax year commencing on or after April 1, 2007.

## (3) Amendments in relation to the application of revised accounting standards

### 1) Finance lease transactions in which title to the lease asset is not transferred to the lessee ("syoyuken iten gai lease transaction")

In August 2002, the Accounting Standards Board of Japan (ASBJ) began its review of the previous "Accounting Standards for Lease Transactions". On March 30, 2007, the ASBJ released new "Accounting Standards for Lease Transactions and its Implementation Guidance" ("New Guidelines"), that will be applicable for the years commencing on or after April 1, 2008.

Under the previous "Accounting Standards for Lease Transactions", in general some leases are treated as "operating" leases (generally current expense of payments) and others as "finance" leases (generally treated as a purchase of an asset with financing). However, under certain circumstances corporations are allowed to treat what would typically be considered finance leases, as operating leases. This occurred in certain cases in which the title to the leased asset was not transferred to the lessee in a manner similar to "operating lease" transactions. Under the New Guidelines, these kinds of leases will be accounted for as finance leases.

Under previous corporate tax law, "finance lease transactions" which satisfy any one of the statutory requirements set out below are treated as sales transactions (of the leased asset) rather than as an operating leasing transaction.

- (i) title to the leased asset is transferred to the lessee for nominal value;
- (ii) the lessee is granted a discounted purchase option to the leased asset;
- (iii) the leased asset is designed specifically for the lessee's business use ; or
- (iv) similar transactions.

Where any of the above "finance lease transactions" take place, title to the leased asset is retained by the lessor during the lease term.

However, in a sale and lease back transaction, the sale of the leased asset at the beginning of the lease is disregarded if such lease transaction is recognized as financing from the substance of the transaction.

Under the 2007 Tax Reform, for tax purposes leases which are treated as finance lease transactions for accounting purposes in which title to the lease asset is not transferred to the lessee at the end of the lease term ("syoyuken iten gai lease transaction") would be treated as follows:

- a) The lease transaction would be treated as a sale rather than a lease (i.e., for tax purposes, the

asset is deemed transferred to the lessee while the title to the asset is retained by the lessor).

- b) The lessee would depreciate the lease asset using the straight line method for tax purposes, even if the lessee recognizes the lease expenses rather than depreciation for accounting purposes.
- c) The lessor would recognize the profit realized from the lease transaction (gross lease income less the acquisition cost of the lease asset) in the following way:
  - i) the amount equivalent to the interest portion (approximately 20% of the profit realized from the lease transaction) would be allocated over the lease term pursuant to the interest method, and
  - ii) the rest of the profit would be recognized equally over the lease term.
- d) For leases entered into before April 1, 2008, the lessee would be allowed to depreciate the lease asset over the life of the lease term using the straight line method for the fiscal years ending on or after filing the notice to the relevant tax office.

The above amendments a), b) and c) will be applicable to finance leasing transactions entered into on or after April 1, 2008.

## 2) Measurement of inventories

New accounting standards for the "Measurement of Inventories" (ASBJ Statement No.9) will be applicable to the fiscal years beginning on or after April 1, 2008 (by election, a corporation is able to apply the new accounting standards earlier). Under the new standards, the lower of cost-or-market method will become the default method for the measurement of inventories at the fiscal year end. With regard to inventories held for sale in the ordinary course of business, if the net selling value falls below the book value at the fiscal year end, the inventories shall be carried at the net selling value on the balance sheet. The net selling value in this context is defined as the selling price less additional estimated manufacturing costs and estimated direct selling expenses. Once a writedown to market has occurred, a corporation has a choice between applying the "reversal method" or the "non-reversal method" to the written down amount.

Under the new accounting standards, inventories held for trading purposes must be carried on the balance sheet at market price and the difference between market price and book value should be treated as profit or loss for the fiscal year.

Under previous tax law, "market" for purposes of the lower of cost-or-market method is the replacement cost (on a raw material basis)

At the time the new accounting standard is applied for accounting purposes, we understand that the 2007 Tax Reform will provide that accounting for inventories for tax purposes will follow the accounting rules.

Inventories held for trading purposes shall be valued based on the market price at the year end.

The above amendments are applicable to the tax year commencing on or after April 1, 2007.

## **2. Measures Supporting Small- and Medium-Sized Corporations (SMC) and Venture Capital Corporations (VCC)**

### (1) Preferential tax treatment for capital gains on the transfer of shares in qualified SMC and VCC

Under the previous tax law, preferential treatment for capital gains on transfer of shares in a qualified SMC or VCC includes:

- 1) A deduction for the acquisition costs of the shares from any capital gain;
- 2) A carryforward of any capital loss for three years; and

3) A reduction in the amount of capital gain subject to the taxation of one half of the actual gain.

The 2007 Tax Reforms, as illustrated below, are intended to provide additional incentives for investing in SMC and VCC shares.

a) The scope of qualified SMCs and VCCs is broadened.

- Newly incorporated companies which are one year old or less, which otherwise qualify as an SMC or VCC, need only to satisfy the developing activities requirement and not the research activities requirement in order to benefit from the preferential tax treatment.
- Newly incorporated SMCs or VCCs that have been in existence for one year or longer but less than two years can be a qualified corporation for purposes of the preferential tax treatment, to the extent that the number of personnel engaged in the developing activities satisfies the statutory requirements even if the company does not satisfy some of the research activities requirements.
- SMC or VCC existing for two years or longer but less than five years can be a qualified corporation for purposes of the preferential tax treatment to the extent that the sales growth ratio is at least 25%, even if it does not satisfy the statutory requirement for R&D expenditures.
- The number of employees required for a company to be treated as a qualified corporation to revitalize a specific region is reduced from 20 to 10.

b) Filing a confirmation with the METI for qualified SMC or VCC status

- Under the current statutes, a corporation must file a confirmation with the METI as to its SMC or VCC status every time it has a new capital infusion. In addition to this procedure, it is proposed that a corporation should be able to file a confirmation in advance of the beginning of every year.

c) The preferential tax treatment to reduce to one-half the capital gain amount that is subject to tax will be extended for another two years.

The above amendments are applicable to the tax year commencing on or after April 1, 2007.

(2) Family corporation surtax

Under the 2007 Tax Reform, a corporation with paid in capital of 100 million yen or less is exempt from the family corporation surtax that is imposed on excess retained earnings.

The above amendments are applicable to the tax year commencing on or after April 1, 2007.

(3) Special depreciation or tax credit for qualified assets acquired by an SMC

An SMC that acquires qualified machinery and equipment is allowed to elect to claim either a special depreciation or tax credit. It is proposed that this special treatment should also be applicable to certain other kinds of machinery and equipment if the SMC engages in the business of promoting the utilization of regional resources in accordance with the relevant law of which the applicable period is extended for another 2 years.

(4) Valuation method for certain non-traded stocks

By the 2007 tax reform, a valuation method was established for inheritance tax and other tax purposes for certain non-traded stocks that are expected to be utilized as a vehicle for inheritance including:

- 1) Preferred stocks without voting rights
- 2) Stocks similar to bonds
- 3) Stocks with veto rights

The above amendments are applicable to the shares inherited to the shareholder of family-owned corporation on or after January 1, 2007.

### **3. Amendments Relating to the Enactment of the Corporate Reorganization Provisions under the Corporation Law**

#### **(1) Consideration paid to shareholders in a corporate reorganization**

The new Corporation Law rules relating to corporate reorganizations become effective as of May 1, 2007. These rules allow more flexibility for corporations carrying out merger and acquisition transactions and will enable acquiring companies to acquire a target corporation in Japan via the so-called “triangular merger”. In a triangular merger, a corporation exchanges the stock of its parent company for shares of a target company.

The 2007 Tax Reform provides that a corporate reorganization in which shares of the parent corporation (domestic or foreign) are exchanged by a Japanese acquiring corporation solely for the shares of a Japanese target corporation will be treated as tax qualified only if (1) the parent directly owns, and will continue to own, 100% of the shares of the Japanese acquiring corporation prior to, and after, the reorganization and (2) any one of the other requirements for a tax qualified reorganization are met (e.g., the continuity of business test – see other articles regarding the requirements for a tax qualified reorganization).

Under the 2007 Tax Reform, if shares of a foreign parent are issued to a non-resident shareholder of the target Japanese corporation, the non-resident shareholder upon receiving the new shares will be subject to capital gains taxation based on the application of Japanese tax laws and any relevant income tax treaty. In other words, the non-resident will be subject to Japanese taxation if

- (a) the non-resident has owned 25% or more of the Japanese target company within the past three years and disposes of 5% or more of such shares in a taxable year, and
- (b) the non-resident is resident in a country that has not concluded a tax treaty with Japan or the relevant tax treaty does not exempt capital gains taxation in Japan upon a share transfer.

The above treatment is not applicable if such shares are attributable to a permanent establishment (PE) in Japan of such non-resident shareholders. In such a case, the capital gain is deferred until such time when the shares are no longer maintained by the PE in Japan in which case there is a deemed transfer of shares by the non-resident shareholder which is subject to taxation.

In a triangular merger, an acquiring company will transfer stocks of the parent company to shareholders of the target in exchange for shares of a target company. By the 2007 Tax Reform, the acquiring company will be required to recognize built-in gain or loss of the parent’s shares held on or before the date of the reorganization contract.

The 2007 Tax Reform also expands the definition of the business relevancy to be met for the reorganization between the parties with 50% or less equity relationship. By the amendment, the business includes preparatory activities like market research or advertisement. The above amendments apply to corporate reorganizations carried out on or after May 1, 2007.

#### **(2) Measures to cope with the abusive use of cross border merger and acquisition transactions**

In relation to the above amendments, the legislation against abusive use of cross border mergers and acquisition transactions is proposed as follows:

- 1) It is proposed that for intra-group reorganizations, if the foreign parent (which issues new shares upon the corporate reorganization in Japan) is a shell corporation located in a tax haven country and the Japanese acquiring corporation does not carry out any business in Japan, the transaction will be treated as a tax disqualified reorganization. As a result, the shareholders of the acquired corporation will not be allowed to defer capital gains resulting from the disposal of shares owned prior to the reorganization (e.g., shares of merged corporation).

The above amendment will be applicable to corporate reorganizations carried out on or after May 1, 2007.

- 2) If a Japanese corporation contributes shares of controlled foreign corporations (“CFC’s”) that are subject to anti-tax haven taxation (i.e., generally subject to a tax rate of 25% or less) to the following type of CFC, such contribution will be treated as a tax disqualified reorganization.
  - (i) a shell company located in a tax haven country where 80% or more of its equity is held by a Japanese corporation, or
  - (ii) a subsidiary of a corporation described in (i)

The above amendments will be applicable to a contribution in kind that is carried out on or after October 1, 2007.

- 3) As a result of a corporate reorganization, if a Japanese shareholder comes to own 80% or more in a Japanese corporation via a shell company located in a tax haven company, the retained earnings (in proportion to the percentage of the equity ownership) of the shell company will be added to the taxable income of the Japanese shareholder. The Japanese corporation subject to the above new rule is limited to corporations owned by a small number of shareholders.

The above amendments will be applicable to the cases where shareholder(s) take control of a Japanese corporation via a foreign corporation on or after October 1, 2007.

#### 4. International Taxation

##### (1) Entities subject to Anti-Tax Haven taxation

Foreign corporations which are subject to the Japanese tax haven rules for the aggregation of income are “foreign related corporations”. Foreign related corporations are those foreign corporations which have more than 50% of their issued shares held either directly or indirectly by residents of Japan or Japanese corporations (sometimes, these are referred to as “controlled foreign corporations” or “CFCs”). Furthermore, if Japanese corporations establish overseas trusts which are similar in nature to “specified trusts” (*tokutei shintaku*), then the income retained in these trusts will also be subject to the income aggregation rules.

Japanese corporations affected are those which either own directly or indirectly at least 5% of the issued share capital of the foreign related corporation, or which are members of family shareholder groups with such holdings.

Under the previous rules, the 5% threshold is determined by the number of shares with voting rights (in relation to the distribution of surplus) or shares with rights to earnings of total shares outstanding. When a foreign corporation issues several classes of shares, it is not clear how to determine if the 5% threshold is met.

Under the 2007 Tax Reform, the 5% threshold should be determined by the largest percentage of each class of shares (shares with voting rights or shares with rights to earnings) or the amount of earnings the Japanese shareholder is able to claim for distribution upon exercising its rights.

##### (2) Statutory requirements to be exempt from the anti-tax haven taxation

Under the previous anti-tax haven rules, where a CFC has the characteristics of an independent enterprise and there is a sufficient economic rationale for carrying out operations in the country of the CFC’s head office or principal place of business, the CFC’s undistributed income may be exempted from Japanese tax, provided that all of the criteria (business purpose test, substance test, management and control test, and unrelated party test or country of location test) are met.

Under the 2007 Tax Reform, the above exemption is not applicable if the taxpayer does not keep certain required documentation.

The above amendments are applicable to the undistributed income of the CFC for the year ending on or after April 1, 2007.

(3) Request for downward correction as a result of successful mutual agreement procedures

Under the 2007 Tax Reform, at the conclusion of a successful mutual agreement procedure any resulting transfer pricing adjustment or other tax adjustment must be carried out by making a request for a downward correction. A taxpayer would be required to follow this procedure for tax liabilities incurred during the period the mutual agreement is concerned.

The above amendments are applicable for any request for a downward correction that is filed for the income of the fiscal year beginning on or after April 1, 2007.

## 5. Transfer Pricing Legislation

Deferral of tax payment and exemption from delinquent tax in relation to mutual agreement procedures

In the event that a taxpayer files a request for mutual agreement procedures following a transfer pricing assessment, payment of national tax and penalties pertaining to the assessment can be deferred until the completion of the mutual agreement procedures (one month after the day following the date of reassessment based on the mutual agreement, or, should agreement not be reached, one month from the day following the notification of this fact to the taxpayer), if requested by the taxpayer. The taxpayer, however, needs to provide collateral for the amount of taxes to be deferred. In addition, the taxpayer is exempted from delinquent tax for the deferral period.

The above amendments are applicable for requests filed on or after April 1, 2007.

## 6. Tax System Changes Related to Trust Law Reform

(1) Reform in the Japanese tax system relating to trusts is implemented along with the introduction of a Trust Law Reform with respect to the following types of trusts: (i) Trusts Issuing Beneficiary Securities, (ii) No Beneficiary Trusts, and (iii) Trusts Allowing Continual Change of Beneficiary)

1) Trust Issuing Beneficiary Securities

- a) The revenue and expenditure attributable to the trust assets of a Specified Trust issuing Beneficiary Securities are not taxed at the trustee level. However, the distribution of profit received by a beneficiary is subject to individual income or corporation tax.

A Trust Issuing Beneficiary Securities which meets, amongst others, the following conditions set out below is recognized as a Specified Trust Issuing Beneficiary Securities.

- The trustee is a corporation that has obtained approval from the director of a tax office
  - Undistributed profit of the trust is 2.5% of the total amount of trust principal or less
  - Computation period of the trust is not over one year, etc.
- b) With regard to a non-Specified Trust issuing Beneficiary Securities, corporation tax is imposed on a trustee's income arising from trust assets separately from the income arising from its own assets.
  - c) A distribution of profit received by an individual beneficiary of a non-Specified Trust issuing beneficiary securities are subject to individual income tax, as dividend income and the income arising from the transfer of such beneficiary securities are subject to individual income tax as capital gains on stock.
  - d) Beneficiary securities under a Trust Issuing Beneficiary Securities are subject to stamp tax.

## 2) No Beneficiary Trust

With regard to No Beneficiary Trusts, corporation tax is imposed on a trustee's income arising from the trust asset separately from the income arising from its own assets. In addition, when a No Beneficiary Trust is created, the settlor is subject to taxation on the deemed transfer or donation taxation and a trustee is subject to taxation on the donated gain against the amount equivalent to the trust asset.

## 3) Trust Allowing Continual Change of Beneficiary

Under a Trust Allowing Continual Change of Beneficiary, the beneficiaries at the time of creation and thereafter are deemed to acquire a beneficiary certificate from the settlor or the preceding beneficiary as appropriate and are subject to inheritance tax, etc.

(2) It was introduced that a rationalization measure be implemented with regard to tax avoidance which arises by using a trust structure. Corporation tax is imposed on a trustee with regards to a trust entrusted by a company as settlor if one of the following conditions is met:

- Where "all or primary part of the business" is entrusted and more than half of the beneficial certificates are to be transferred to its shareholders
- Where the trust term of a Trust created by Declaration is more than 20 years (excluding trusts where the useful life of primary depreciable assets entrusted is more than 20 years etc.)
- Where the beneficiary certificates of a Trust created by Declaration are owned by a special related person such as its subsidiary etc. and the distribution ratio of profits or losses is variable

(3) Implementation of rules on trust beneficiaries with regard to utilization of trust losses.

(4) In the case of a merger or division of a Proviso Trust, being one of the forms of investment trust whereby no title to property other than a beneficial certificate of the new trust can be transferred, realization of the profit or loss on the beneficial certificate of the original trust can be carried forward to a later date.

(5) With regard to the issue as to the taxable residence of a trust, the 2007 Tax Reform provides that a trust entrusted at a domestic office in Japan is taxed as a domestic company and a trust entrusted at a foreign office is taxed as a foreign company.

(6) The 2007 Tax Reform provides clarification of the definitions regarding (i) joint operation trusts, (ii) when a trust beneficiary should be treated as having an interest in a trust asset and (iii) the scope of grantor which is subject to trust rules.

The above amendments are applicable for trusts effectuated on or after the new Trust Law become effective.

## 7. Reporting Requirements and Withholding Tax Systems for Kumiai Business

The provisions relating to the reporting requirements and withholding tax systems for a Kumiai Business are amended as follows:

- (1) With regard to profits or losses which belong to the Partners of an Investment Limited Partnership, a system of submitting account statements will be introduced in addition to the existing "Accounting Statement of Partners Income for Limited Liability Partnership" which is already provided to the Partners.
- (2) The recipients (i.e. nominees) who receive consideration relating to transferred shares on behalf of the investors in a Kumiai Business will be required to file a record of the transferred shares with the tax office on or before January 31 of the following year.

- (3) With respect to withholding tax on Tokumei-Kumiai (“TK”) profit distributions, the requirement regarding the number of TK investors who conclude a TK contract with a TK operator is removed. Therefore, all distributions of profits to TK investors, including Japanese residents and resident corporations, will be subject to payment record submission and withholding tax.
- (4) The above treatments will be applicable to profit distributions based on a TK contract and the submission of account statements reporting on or after January 1, 2008.

## 8. The Tax System on Finance and Corporate Securities

### (1) Preferential Tax Treatment for Dividend Income on Listed Stocks

The preferential tax treatment for dividend income on stocks listed on a Japanese stock exchange (national tax 7%, local tax 3%) is extended for one year until March 31, 2009.

### (2) Preferential Tax Treatment for Capital Gains on Listed Stocks

The preferential tax treatment for capital gains on stocks listed on a Japanese stock exchange (national tax 7%, local tax 3%) is extended for one year until December 31, 2008.

### (3) Special Tax Treatment for Deemed Dividends

The special tax treatment on a deemed dividend realized where a company purchases its own shares from the market in a certain way (*kokai kaitsume*) is extended for two years until March 31, 2009.

### (4) Exemption from Withholding Tax Imposed on Redemption Gains from the Issuance of Short-term Bonds Issued by an Investment Corporation

The exemption from withholding tax imposed on redemption gains from issuance is extended to cover the short-term bonds issued by an investment corporation.

### (5) Deduction for life insurance premiums

The deduction for life insurance premiums is applied to contracts relating to certain mutual life insurance products concluded with specified mutual aid associations and specified federations of mutual aid associations under the cooperative union law of medium and small companies.

## 9. Other Amendments

### (1) Tax incentives to promote the e-filing of tax returns

#### 1) Tax credit for e-filing tax returns

An individual taxpayer who files a tax return by e-filing for the taxable year of 2007 or 2008 is able to claim a tax credit up to 5,000 yen for one year (either 2007 or 2008 only) if certain requirements are met. This amendment is applicable for tax returns filed on or after January 4, 2008 for the tax year of 2007. An individual taxpayer who files before January 4, 2008 for the 2007 tax year and departs from Japan is able to get a refund by filing the claim of downward correction within one year from the filing date.

#### 2) Tax credit for registration and license tax upon online application for registration

Those who filed registration applications as listed below via a website between January 1, 2008 and December 31, 2009 can claim a tax credit in an amount equal to 10% of the registration and license tax, up to 5,000 yen.

- a) Title transfer of real estate or placing a security interest on the real estate; and
- b) Incorporation of Kabushiki Kaisha, etc.

## (2) Specific donation to certain qualified entities

It is amended that a “donor” who makes a donation to a specific entity (which carries out business to secure the employment for handicapped persons or to foster human resources for future generations) is able to claim a special donation deduction. A donor includes a corporation, individual and an inheritance beneficiary.

### 1) Corporate donor

- Such donations are treated as similar to donations to specified entities that promote public interests (*Tokutei Koueki Zoushin Houjinn*) and a donor is able to claim a deduction, subject to limitations that is provided separately from the limitation for general donations.

### 2) Individual donor

- Such donation is deemed as a designated donation under the Income Tax Law and the donor is able to claim an income tax deduction.

### 3) Individual donor who inherited certain property

- A donation of inherited property is not subject to the Inheritance Tax unless such donation is carried out for the purposes of tax avoidance.

## (3) Preferential treatment of stamp duty on certain contracts

The 1997 Tax Reform reduced the applicable stamp duty tax rate on contracts for the transfer of real property or for construction. Under the 2007 Tax Reform, the preferential treatment is extended for another two years.

## (4) Extension of exemption of stamp duty on securities issued upon certain corporate reorganizations

The 1993 Tax Reform exempted securities issued upon certain corporate reorganizations from stamp duty. Subsequent legislation expanded both the type of securities and the nature of the transactions subject to the exemption. Under the 2007 Tax Reform, the exemption is extended for another two years.

## (5) Deduction for contributions

For individual income tax purposes, the restriction on the allowable amount for contributions is increased from to 40% from the previous 30% of the taxpayer's total income amount.

## 10. Individual Tax

On January 11, 2007, Japan and France signed the “Protocol Amending the Convention Between the Government of Japan and the Government of France for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income”. The Protocol enables deductions for income tax purposes of the resident country for the social insurance premium paid under the Social Security regime of the contracting country. In accordance with the enactment of the Protocol, by the 2007 Tax Reform, the income tax treatment is amended as follows:

- (1) Japanese residents are able to claim deductions subject to certain limitations from gross income reported in Japan the social insurance premium paid under the social security regime of the contracting state (i.e., France).
- (2) Japanese non-residents are able to claim deductions subject to limitation from salary income or domestic source income reported in Japan the social insurance premium paid under the social security regime of the contracting states (i.e., Japan and France).

The above amendments are applicable for the social insurance premium paid on or after April 1, 2007.

You have a vision. PricewaterhouseCoopers helps bring that vision to reality. We hope you enjoy the current issue of Japan Tax Update and appreciate your comments or ideas for what you'd like to see covered in future issues.

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