

## **FY2011 Tax Reform (Main Points)**

Ministry of Finance

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(Provisional translation)

### **Measures to facilitate tax compliance and enforcement**

1. The government will make the largest review on the Act on General Rules for National Taxes since its enactment in 1962. The measures will include: introduction of “Taxpayers’ Charter”; clarification of tax audit process; extension of the limitation period for taxpayer’s request for reassessment; and notification of grounds for administrative disposition.
2. As for the reform of National Tax Tribunal, the government will consider reviewing administrative appeal procedures, and the tribunal’s organization and the personnel system, while taking into account the direction of entire review on the administrative appeal system.
3. With the aim to swiftly introduce single identification number system, the government will facilitate its study mainly at the “Panel on Identification Number System for Social Security and Tax”. Related issues in the tax system such as expanding the scope of statutory information returns will also be examined proactively.

### **Individual income taxation**

4. A standard upper limit on the deduction for employment income (JPY 2,450,000) will be introduced and will be applied to person earning more than JPY 15,000,000 of employment income.
5. The deduction for employment income will be reduced for executive’s high compensation as follows:
  - For executives earning over JPY 40,000,000 of employment income, the upper limit on the deduction for employment income will be reduced to a level equivalent to half of the standard upper limit of the deduction (JPY 1,250,000)
  - For executives earning between JPY 20,000,000 and JPY 40,000,000 of employment income, the deductible amount will be reduced gradually in inversely proportion to employment income until it reaches JPY 1,250,000. In certain employment income range in the between, the upper limit of deduction will be fixed at a level equivalent to 3/4 of the standard upper limit of deduction.

6. The scope of specific expenses allowed for deduction will be expanded to cover wider range of expenses so that employees have more opportunity to claim actual expenses for deduction.
  - Specifically, the following expenses are added to the scope of specific expenses deduction: expenses for obtaining certain qualifications such as attorneys, CPAs, tax accountants and etc.; business expenses (for instance, expenses for books and clothing, social expenses, business-related membership fees).
  - The specific expenses deduction can be claimed if it exceeds a level equivalent to 50% (instead of 100% at present) of the standard amount of the deduction for employment income.
7. The income deduction applied to retirement allowance will be abolished for short-term executives (whose term is 5 years or below). The 10% tax credit of individual inhabitant tax will be abolished for retirement income.
8. The exemption for adult dependents will be reduced as follows, based on the view that adults should earn their living by themselves in principle:
  - The exemption will be sustained with regard to dependents who are handicapped, certificated for long-term care, difficult to work due to mental or physical disorder, aged more than 64 years or students.
  - The exemption will be sustained for taxpayers with employment income JPY 5,680,000 or less, regardless of the dependent's situations, in consideration of taxpayer's financial burden of supporting dependents.
  - Starting from employment income JPY 5,680,000, the exemption will be reduced gradually as employment income increases. The exemption will be abolished completely for taxpayers earning more than JPY 6,890,000.

(Note) Under the present system, the exemption is uniformly applied with regard to dependents that are from 23 to 69 years old.
9. The measures will be taken to ease the filing burden of pension recipients who receive JPY 4,000,000 or less of public pension and earn JPY 200,000 or less of other income.
10. The current preferential treatments to apply reduced tax rate (10%) for dividend and capital gain on listed stocks will be extended for 2 years. The tax rate will be raised to statutory rate (20%) from January 2014. Together with these conclusions, the introduction of so-called Japanese ISA will be postponed to January 2014.

## **Property taxation**

### **Inheritance taxation**

11. The basic deduction for inheritance tax will be reduced from "JPY 50,000,000 + JPY 10,000,000 × the number of statutory heir" to "JPY 30,000,000 + JPY 6,000,000 × the number of statutory heir".
12. The structure of inheritance tax system will be revised, e.g., the maximum tax rate will be raised from 50% to 55%.
13. The non taxable limit applied to life insurance calculated by "JPY 5,000,000 × number of statutory heir" will be changed to "JPY 5,000,000 × the number of statutory heir fulfilling either of the following conditions".
  - a. minors under the age of 20
  - b. handicapped
  - c. those who lived in the same household immediately before the time of inheritance
14. The inheritance tax credit for minors (JPY 60,000 × the number of years left until reaching the age of 20) and the inheritance tax credit for handicapped (JPY 60,000 × the number of years left until reaching the age of 85) will be increased to JPY 100,000 respectively.

### **Gift taxation**

15. The tax rate structure of the gift tax regarding the calendar year taxation will be relaxed where the donee is a lineal descendant of the donor and is 20 years old or older.
16. Regarding the special system in which gift tax can be deferred and adjusted with inheritance tax at the time of inheritance, grandchildren 20 years old or older are added to the donee applicable to the system, and the system's requirement on age of the donor will be relaxed from "65 years old or older" to "60 years old or older".

## **Corporation taxation**

17. The effective corporate tax rate, which includes national and local taxes, will be reduced by 5% in order to promote domestic investment and job creation through enhancing Japanese companies' international competitiveness as well as improving the environment for business establishment [40.69% ⇒ 35.64% (Tokyo)]. For this purpose, the statutory corporate tax will be reduced from 30% to 25.5% by 4.5%.
18. The preferential corporate tax rate for SMEs will be reduced from 18% to 15% by 3%.
19. In conjunction with the reduction of the effective corporate tax rate, the tax-base broadening measures will be taken in order to obtain revenues. The measures include

review of the Special Tax Measures (e.g., abolishment and reduction of the special measures for depreciation and reserves), review of the depreciation speed, limitation on the loss carryover for large corporation, and etc.

20. In order to promote employment and investment, the following measures will be introduced; a new tax credit applicable to companies which increase employment to a certain extent (JPY 200,000 multiplied by the number of increased employees) (Employment Enhancing Tax System); special depreciation and tax credit for advanced low-carbon and energy-saving equipments, special depreciation, tax credit and income deductions in the International Strategic Special District (tentative title) which targets big cities with competitive advantages internationally, and income deductions which aim to attract global companies' R&D centers and Asian regional headquarters.
21. In order to make a thorough review of the Special Tax Measures, 109 items of tax expenditures were reviewed, and, as a result, 50 items will be abolished or reduced.

#### **Consumption taxation (Taxation on energy)**

22. The government will introduce "Carbon Dioxide Tax of Global Warming Countermeasure" with the aim of controlling the emission of energy-originated CO<sub>2</sub> which accounts for about 90% of greenhouse gas causing global warming.

The government will add following tax rates corresponding to the amount of CO<sub>2</sub> emission on the petroleum and coal tax on fossil fuel.

Added tax rate: -Crude oil, petroleum products: JPY 760/kl (at present: JPY 2,040/kl)

-Gaseous hydrocarbons: JPY 780/t (at present: JPY 1,080/t)

-Coal: JPY 670/t (at present: JPY 700/t)

The introduction of new tax will be enforced on October 1, FY2011. Necessary interim measures will be taken until March 31, FY2015.

23. The government will reduce the rate of aviation fuel tax to JPY 18,000/kl (at present: JPY 26,000/kl) from FY2011 to FY2013. The government will also reduce the tax rates for Okinawa route (tax rate reduced to 1/2) and solitary islands route (tax rate reduced to 3/4) with the same ratio. The government will increase the rate of aviation fuel transfer tax to 2/9 (at present: 2/13) from FY2011 to FY2013.

#### **Tax system for nonprofit organization**

24. The government will introduce new tax credit for income tax with respect to donations made to certified nonprofit corporations (the rate of deduction is 40%; 50% will be deducted together with personal inhabitant tax). Comparable tax credits will be introduced for donations to public interest incorporated association and foundation,

educational institution, social-welfare-service corporation, and relief- and rehabilitation-service corporation.

25. The requirements for certified nonprofit corporations will be relaxed; e.g., the number of donors (a hundred or more donors donating over JPY 3,000 per year) will be available as a measure for PST (Public Support Test).

The government will also take necessary tax measures when a new system of certification currently under examination (introduction of local government's certification, provisional certification system etc.) is legally introduced.

26. The government will enhance its support to specified nonprofit corporations by expanding the scope of donation applicable to tax credit for personal inhabitant tax.

#### **Local sovereignty reform and local taxation system**

27. In order for the local government to play its enough role in the promotion of "local sovereignty reform", the government will enrich local taxes and will build a local tax system, in which tax sources are evenly distributed among local governments and tax revenues are stable.
28. The government will take forward a drastic reform of the local tax system towards expanding "independent judgment" and "responsibility of execution", and will carry out definite plans as soon as they are obtained.
29. From the viewpoint of "local sovereignty reform", the government reviewed 100 items of tax expenditures, and, as a result, will abolish or reduce 64 items.