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Japan tax alert

Ernst & Young Tax Co.

New growth strategy and corporate tax reform

On 24 June 2014, the Japanese government adopted a new growth strategy and "the basic policies for economic and fiscal policy management and reform ("the basic policies") at a cabinet meeting. On 27 June 2014, the government's Tax Commission also gave approval to the report regarding corporate tax reform entitled "About Corporate Tax Reform" (hereinafter, the "Report") and then outlined its proposals over future corporate tax reform.

"Growth strategy," which is one of the "three arrows" of Prime Minister Abe's government, is finally moving into the execution stage through corporate tax reform and the reform of "hard-rock regulations," which have been presented by the basic policies. The government unveiled a policy to cut the effective corporate tax rate from the current roughly 35 percent to below 30 percent over several years starting in the next fiscal year.

The Report of the government's Tax Commission, which was released immediately after said adoption, describes the purpose of corporate tax reform and proposes detailed reform areas. In order to strengthen Japan's corporate competitiveness by enhancing its "locational" competitiveness, the necessity to lower its corporate tax rate has been stressed. The Report also states that lowering the tax rate with the enlargement of the taxation base would contribute to changing the structure of the corporate tax system in which a "lighter" tax burden is shared by "broader" sources. It also indicates that corporate tax reform will not necessary have to be revenue neutral including other tax items, whereas consideration is given to compatibility with financial restructuring.

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The detailed reform areas as proposed by the government's Tax Commission show measures to secure an alternative source of tax revenue with the tax cut (lowering the effective corporate tax rate). The Report says that as long as lowering the effective corporate tax rate is a permanent tax cut measure, it is a hard-and-fast rule to prepare permanent tax revenue. The detailed reform areas include the following items:

- Revision of tax incentives provided based on Special Taxation Measures Law (including R&D tax credit regime)
- Revision of NOL carry-forward system (extension of carry-forward periods and revision of upper cap of current NOL deduction)
- Revision of dividend exemption system (revision of applicable conditions)
- Revision of depreciation system (unification to the straight-line method)
- Revision of local tax deductions for national corporate tax purposes
- Revision of taxation of small and medium sized companies (revision of several tax benefits)
- Revision of taxation on public interest corporations
- Revision of local corporate taxation (revision of business scale taxation on corporate enterprise tax)

In addition, the revision of international taxation in response to the OECD's BEPS project and consideration of employment income deductions for individual income tax purposes are listed as matters to be discussed in line with corporate tax reform.

Further deliberation will be made toward the end of the year with regard to the implementation and execution of these measures at discussions regarding next fiscal year's tax reform.

Comments or general inquiries regarding this tax newsletter may be directed to our Corporate Communications team at tax.marketing@jp.ey.com.