

Investing in Japan

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1. How does your jurisdiction compare internationally as a destination for inward investment?

Foreign direct investment (FDI) into Japan remains very low in absolute terms, in particular in relation to GDP and compared to the rest of the world. Aside from a peak in 2007 and 2008 where FDI inflows exceeded US\$20 billion in each year on the back of a global mergers and acquisitions (M&A) boom, inbound FDI in the last decade has been negligible, and indeed suffered net outflows in four of the last eight years. Net inflows in 2013 were US\$2.3 billion, up marginally from US\$1.7 billion the previous year. Total FDI stock in Japan stood at just US\$171 billion at the end of 2013.

The Japanese economy has suffered from low growth and deflation in the last decade, and is therefore not seen as an attractive destination for growth capital, particularly in relation to other countries in Asia. Japanese companies also prefer to seek growth outside of Japan, and in 2013 made US\$136 billion of outbound direct investments, the second highest in the world after the US. Japan currently has a stock of over US\$1 trillion direct offshore investments.

There are perceived to be a number of obstacles to foreign-affiliated companies operating in Japan, including, among others:

- High business costs.
- High rates of taxation.
- Strict licensing and regulation.
- Difficulty in securing human resources.
- Lack of incentives.

In addition, a number of structural impediments remain with respect to the execution of M&A transactions, which are an important mode of inbound investment in developed markets.

Japan remains an attractive destination for portfolio investments. The Tokyo Stock Exchange is the third largest stock exchange in the world, with a market capitalisation of over US\$4 trillion. Foreign ownership of listed stocks accounted for 31% of shares listed on Japan's four exchanges at the end of March 2013, the highest level ever, and up from 28% in the previous year. Trading by foreigners accounts for around half of turnover in terms of both volume and value.

2. What types of companies are attracting foreign investment into your jurisdiction and what are the most active sectors?

A large amount of direct investment occurred in Japan between 1998 and 2002, driven by global market factors coupled with deregulation in certain industries in Japan. The focus of the boom was within a specific set of industries, including finance and insurance,

wholesale and retail, and the machinery industry in the manufacturing sector. These industries still hold the largest stocks of foreign investment today. One anomaly is the telecommunications industry, which received significant foreign investment, but which is now firmly back in Japanese ownership.

Foreign buying of listed stocks in anticipation of reforms by the Abe government was a key driver of the 57% increase in the Nikkei average in 2013. Net purchasing by foreigners was as much as JPY15 trillion, while Japanese individuals and corporations were net sellers. Foreign buying was particularly strong in companies with global operations expected to benefit from a weaker yen, such as Seiko Epson, Dentsu and Shiseido. Similarly, companies with mainly domestic operations and a strong reliance on domestic demand, such as KDDI, Mitsui Real Estate and Seven & i Holdings, saw a strong increase in foreign ownership.

3. What will be the main factors affecting the market and how do you expect the market to develop?

Investor confidence in structural reform and the extremely accommodative monetary policy of the Bank of Japan have been the key drivers of the market since the election of the Abe government in December 2012. The strengthening of the government's mandate in the snap election of December 2014, and the effectiveness of government policies in effecting structural change following the election, will play a significant role in how the market perceives the attractiveness of Japan as an investment destination going forward.

The Abe government has targeted a doubling of FDI stock to JPY35 trillion by 2020, which would require a net inflow of around US\$30 billion per year, a tenfold increase from 2013 inflows. The government has announced policy measures, including tax breaks and subsidies for companies, in particular Asian companies, to establish businesses in Japan, among other policies. In addition, a large number of structural reforms are planned to be introduced to encourage inbound acquisitions, such as the implementation of improved corporate governance rules.

A notable current trend affecting inbound direct investment to Japan is the rise of China as an investor. Certain Japanese companies are particularly attractive to Chinese companies, as they possess the advanced standards and technology that Chinese companies require to move up the value chain from a manufacturing based economy. Typical transactions include the joint venture between Lenovo and NEC formed in 2011, and the acquisition of Sanyo Electric operations by Haier Group in 2012. Chinese companies have also recently acquired a number of Japanese brands popular with the increasing number of Chinese tourists to Japan.

LEGAL SYSTEM

4. Please briefly outline the government and legal system.

Japan operates under a civil law system. The Constitution of Japan adopts a representative parliamentary democracy, and provides for separation of powers into three branches:

- The Diet (legislative).
- The Cabinet (executive).
- The Supreme Court (judiciary).

The Diet, whose members are directly elected by citizens, is the highest form of state power and superior to the Cabinet. The prime minister, as head of the Cabinet, is designated by a majority resolution of the Diet.

The House of Representatives, the lower chamber of two chambers, can resolve no-confidence motions with respect to the Cabinet, upon which all Cabinet members must resign from office, subject to the Cabinet's authority to dissolve the House of Representatives. The Constitution provides that all judges must be independent in the exercise of their conscience and are bound only by the Constitution and laws. The Supreme Court is authorised to determine the constitutionality of any law or government action. The Cabinet is responsible for designation of the chief judge and appointment of judges of the Supreme Court. The Diet can establish an impeachment court to try judges.

The Emperor is the symbolic head of state, and does not have any authority or power under the Constitution with respect to state affairs. The Emperor acts in accordance with the advice and approval of the Cabinet for matters prescribed under the Constitution, including, among others, the appointment of the prime minister and the chief judge of the Supreme Court; the calling of the Diet; and the promulgation of laws and regulations.

5. What are the key laws and regulatory authorities governing foreign investment in your jurisdiction?

The Foreign Exchange and Foreign Trade Act (FEFTA) is the main legislation applicable to foreign investments. The Ministry of Finance and the Ministry of Economy, Trade and Industry administer matters related to the Act, alongside the ministries with jurisdiction over specific industries. Under FEFTA, the Bank of Japan also has jurisdiction over certain administrative matters.

6. What international treaty organisations and/or economic, customs or monetary unions or free-trade areas is your jurisdiction a member of?

Japan is a member of the World Trade Organisation. Japan is not a member of any other international treaty organisation, but is currently in negotiation with respect to the Trans-Pacific Strategic Economic Partnership (TPP) and Regional Comprehensive Economic Partnership (RCEP). Japan is also considering a Free Trade Area of the Asia Pacific (FTAAP) proposed by the APEC Business Advisory Council (*see Questions 7 and 29*).

7. What other international agreements apply to foreign investment?

Economic partnership agreements (EPAs)

As of November 2014, Japan has executed economic partnership agreements (EPAs) with Singapore, Mexico, Malaysia, Chile, Thailand, Brunei, Indonesia, Philippines, Switzerland, Vietnam, India, Peru, Australia and the ASEAN (Association of South-East Asian Nations). Such EPAs include rules regarding foreign investments, for example:

- Most-favoured-nation treatment, which provides investors from EPA countries with treatment no less favourable to investors from non-EPA countries.
- National treatment, which provides investors from EPA countries with treatment no less favourable to local investors within the country.

Japan is also currently negotiating EPAs with Mongolia, the Gulf Cooperation Council, the EU, Canada, Columbia, and has recently commenced negotiations with Turkey. Japan is also negotiating a tri-partite agreement with China and South Korea. Bilateral negotiations with South Korea are currently suspended.

Investment agreements

Japan has individual investment agreements with bilateral provisions similar to those contained in EPAs with a number of countries. As of October 2014, Japan has effective investment agreements with Egypt, Sri Lanka, China, Turkey, Hong Kong, Bangladesh, Russia, Mongolia, Pakistan, South Korea, Vietnam, Cambodia, Laos, Uzbekistan, Peru, Papua New Guinea, Kuwait, Iraq, Myanmar, Mozambique, and a tri-partite agreement with China and South Korea. In addition, investment agreements with Columbia, Saudi Arabia, and Kazakhstan have been executed but are not yet effective. Japan is also currently in discussions with respect to investment agreements with Oman, Angola, Ukraine, Algeria, Uruguay, Qatar, the UAE, Kenya, Ghana, Morocco, Libya and Tanzania.

Energy Charter Treaty

Japan has executed an Energy Charter Treaty with the EU and 47 other non-EU countries. The Energy Charter Treaty provides for the liberalisation of international trade and transit of energy source materials and products, and liberalisation and protection of investment in the energy sector.

Tax treaties

As of November 2014, Japan has executed tax treaties with 63 countries and territories. These tax treaties are generally directed towards the avoidance of double taxation and measures against tax avoidance. Japan has also executed tax information exchange agreements with a further ten countries and territories, and the Convention on Mutual Administrative Assistance in Tax Matters with 43 countries and territories to support the administration of tax matters.

INVESTOR INDIVIDUALS

8. Are there any visas, permits or other requirements for foreign individuals entering your jurisdiction for business purposes?

Foreign nationals entering Japan must hold a valid passport and a valid visa, unless a visa waiver applies. As of July 2013, Japan applies a visa waiver to nationals of 66 countries and territories for a short stay of up to 90 days, depending on the country of origin.

Short stay visas prohibit working in Japan, but permit market research and other preparatory activities for future investment. The Japanese Embassy or Consulate General located in the relevant country or territory issue visas for entry into Japan.

In most cases, a Certificate of Eligibility is also required if entering Japan for work or investment purposes. The Ministry of Justice in Japan issues Certificates of Eligibility to applicants approved to work, study or live in Japan.

Visa

Issuance of a work visa usually takes around one to three months. However, this can be shortened to around five business days if the applicant already has a Certificate of Eligibility. Application fees are currently:

- Single-entry visas: JPY3,000.
- Multiple-entry visas (permitting multiple entries within an effective period): about JPY6,000.

The documents necessary for visa applications vary according to the nationality of the applicant.

Certificate of Eligibility for Investors

A foreign national can apply for a Certificate of Eligibility for the purposes of investing in Japan under the category of investment and management. The amount of investment must in principle be at least JPY5 million. The procedures for obtaining this category of Certificate of Eligibility depend on the residential status of the applicant at the time of application. If the applicant does not hold any existing right of residence, an application for a Certificate of Eligibility must be made at the Immigration Bureau with jurisdiction over the place of the prospective residence or prospective employment. No fees are payable for this kind of application. This process usually takes between one and three months.

9. Are there any visa waivers or fast-track procedures available for foreign individuals entering your jurisdiction as investors?

Various benefits in terms of preferential processes for immigration procedures are provided to foreign nationals who are considered highly skilled, for instance in cases where there is no alternative human resource with such skill available in Japan, or for persons who will contribute to the development of a professional or technical labour market. The assessment is made on the basis of a point system, which allocates points to areas such as academic history, career history and annual income.

Benefits for highly skilled foreign nationals include the fast-tracking of an application for a Certificate of Eligibility. This process usually takes around one to three months, but the relevant authority will make efforts to process the application of a highly skilled foreign national within ten days from receipt of the application.

10. What are the circumstances under which an individual becomes liable to pay tax in your jurisdiction? Can individuals be liable for tax on foreign-source income?

Taxation of individuals in Japan depends on the person's status as a resident or non-resident for tax purposes, and, if resident, whether they are a permanent resident or non-permanent resident.

A non-resident is taxed only on domestic-source income. A permanent resident is taxed on worldwide income, while a non-permanent resident is taxed only on domestic-source income and foreign-source income paid in Japan or remitted to Japan from abroad.

A resident is an individual who is domiciled in Japan, or has had residence in Japan continuously for one year or more. A non-resident is a person other than a resident. A non-permanent resident is a resident who does not have Japanese nationality and who has had a domicile or a residence in Japan for not more than five years in total within the past ten years (*Income Tax Act*).

A person's domicile is the location where a person's life is based. If an individual spends significant time in two or more countries, the person's domicile is determined through an objective consideration of a number of factors such as:

- Length of stay.
- Housing arrangements.
- Occupational status.
- Citizenship.
- Location of family.
- Where living expenses are incurred.
- Location of assets.

INVESTMENT RESTRICTIONS

11. Are there any restrictions on foreign ownership and investment in specific industry sectors? Do any formalities, permit or notification requirements apply?

The Foreign Exchange and Foreign Trade Act (FEFTA) restricts investments by foreign investors into:

- Industries which are relevant to national security, public order and public safety. This includes, but is not limited to, the manufacture or mechanical repair of weapons, aircraft, space exploration, nuclear power and products related to those industries, and other general-purpose goods which can be used for military purposes. It also includes electricity, gas, water supply, telecommunications, broadcasting, railway, passenger carriage, and vaccine manufacturing.
- Industries for which restrictions are required for reasons specific to Japan. This includes, but is not limited to, agriculture, forestry, fisheries, petroleum, leather, air transportation and marine transportation.

Any investment into a restricted business would require a before-the-fact filing to be made within the six months before making the relevant investment. This filing is made with the Ministry of Finance as well as any ministries which have jurisdiction over such business, through the Bank of Japan. A thirty-day waiting period applies. The waiting period is often shortened to two weeks, but may also be extended up to five months.

In addition to the restrictions under FEFTA, there may be statutory restrictions on foreign ownership of corporations engaging in specific industries or businesses. The scope of restricted foreign ownership vary according to the relevant statute. For example, under the Civil Aeronautics Act, an air transportation services business can refuse to record the ownership of a relevant foreign individual or corporation on its shareholder registry if one-third or more of the voting rights are to be owned by foreign individuals or corporations. Other statutes include similar restrictions (for example, the Broadcast Act). When contemplating the acquisition of shares in Japanese companies, the specific statute regulating a company's business should be checked in addition to FEFTA.

12. Does the government retain and exercise control over certain industry sectors? If so how?

The government retains and exercises control over some industry sectors in Japan. For example, the gambling industry is currently owned and operated by the government only. Gambling is prohibited in Japan as a criminal offence. Only government-affiliated corporations or local governments are allowed to conduct such business pursuant to specific statute, such as the conduct of horse racing under the Horse Racing Act. The Japanese government is currently contemplating permission for casinos to operate in Japan (*see Question 29*).

The business of mail delivery was deregulated under the Act on Correspondence Delivery by Private Business Operators. As of 31 October 2014, private operators have entered into a limited category of businesses, but the category of business comprising general mail delivery is still only operated by Japan Post Co, Ltd, which is wholly owned by the government.

Private ownership of public infrastructure is currently prohibited by statutes regulating particular assets. However, in September 2011, an amendment to the PFI Law came into force introducing a concession scheme for the private operation of public infrastructure. So far, the concession scheme has been incorporated into legislation regulating airports, and it is expected that it will be applied to other public infrastructure assets such as water, sewerage, toll roads and ports.

13. Are there restrictions on foreign ownership or occupation of real estate? Do any formalities, permit or notification requirements apply?

The Foreign Exchange and Foreign Trade Act (FEFTA) requires the filing of an after-the-fact report of a capital transaction with the Ministry of Finance, through the Bank of Japan, when a non-resident acquires from a resident real property or any right concerning real property, within 20 days from the acquisition. An exception applies where the acquisition is made by a non-resident either:

- For his own residential use or that of his relatives or employees.
- For his use for the purposes of engaging in non-profit business in Japan.
- For his own use as an office. However, the filing would be required if the acquisition is for investment purposes.

Other than FEFTA, there are no national laws that substantially or effectively restrict foreign ownership of real estate. However, local ordinances can require a before-the-fact filing in certain circumstances. For example, Hokkaido Prefecture requires a before-the-fact filing by a seller of certain real property.

14. Are there any minimum capital requirements for foreign investment?

Regulations on financial services and payment services provide minimum capital requirements, minimum net-asset requirements or minimum collateral (by way of deposit, bank guarantee or trust) requirements for the purposes of financial system stability or customer protection. These include the:

- Banking Act.
- Financial Instruments and Exchange Act.
- Money Lending Business Act.

- Insurance Business Act.
- Payment Services Act.

These requirements generally apply equally, irrespective of whether foreign investors invest in the regulated business in Japan. In the case of a branch in Japan of a foreign company, the minimum capital or net assets required must be calculated on a Japan-business basis, (as opposed to a global business basis), and the requisite capital must be maintained within Japan (in other words, capital repatriation is restricted).

15. Are there any exchange control or currency regulations? Are there any restrictions on the remittance of profits abroad?

The Foreign Exchange and Foreign Trade Act (FEFTA) restricts the remittance of money from a resident in Japan to foreign countries in certain circumstances. In certain industries, a remittance requires permission from the Ministry of Finance if it is for the purpose of business activities conducted in a foreign country by a partnership or other organisations established by the remitting residents with other residents or non-residents of Japan, for example:

- Fishery.
- The manufacture of leather or leather products.
- The manufacture of weapons or weapons-related facilities.

Remittance of more than JPY30 million from Japan to foreign countries or from a resident of Japan to a non-resident for other purposes also requires an after-the-fact report to the Ministry of Finance, through the Bank of Japan (and through the bank handling the remittance), unless an exception applies.

In principle, FEFTA requires permission from the Ministry of Finance and the Ministry of Economy, Trade and Industry for the remittance of money to certain parties, such as those designated as terrorists, or for the purposes of contributing to nuclear activities. In practice this amounts to a prohibition as such permission would be never granted.

IMPORTS

16. Are there any restrictions on the importation of commercial goods and services?

The following are some non-exhaustive examples of statutes that prohibit or restrict the importation of certain categories of goods, for example, by requiring a permission or approval by the relevant authority:

- **The Customs Act.** Goods that are prohibited from being imported to Japan under the Customs Act include:
 - narcotic drug products, weapons, explosive products, gunpowder, chemical substances that can be used for the manufacture of chemical weapons, certain disease agents, forged bills and securities, obscene books and other similar goods;
 - goods infringing intellectual property rights; and
 - goods contributing to unfair competition activities
- **Plant Protection Act.** Specific pests, soil and plants imported from or through specific areas or countries are prohibited for importation to Japan under the Plant Protection Act. Certain plants may also be subject to quarantine, with importation being subject to certification and confirmation by customs authorities.

- **Act on Domestic Animal Infectious Diseases Control.** Infectious diseases are controlled through the prohibition of import of certain goods, or goods from certain areas or countries. Infectious diseases at which prohibition is directed include rinderpest, foot-and-mouth disease, and African swine fever. Other temporary measures may be taken in relation to the emergence of new infectious diseases. Certain animals and livestock products are also subject to quarantine.
- **Act on Ensuring Quality, Effectiveness and Safety of Medical and Pharmaceutical Products and Medical Equipment.** The importation of medical and pharmaceutical products, quasi-drugs, cosmetic products and medical equipment is permitted only with the relevant permission from the Ministry of Health, Labour and Welfare. Similarly, the importation of animal drugs requires permission from the Ministry of Agriculture, Forestry and Fisheries.
- **Food Sanitation Act.** A filing with the Ministry of Health, Labour and Welfare is required for each importation of certain products for sale or commercial use, including food products, food additives, equipment used for processing, storing, carrying, or displaying foods, certain containers and packaging for food and food additives, and certain baby and toddler toys. This documentation must be presented to customs authorities on importation and a quarantine process may be applicable.
- **Foreign Exchange and Foreign Trade Act (FEFTA).** FEFTA prohibits, or requires permission from the Ministry of Economy, Trade and Industry for, the importation of various categories of products including:
 - goods for which the volume of importation is limited and allocated between certain importers by the Ministry of Economy, Trade and Industry, for example certain fish, shellfish and seaweed;
 - shipments from certain countries or countries of origin, such as salmon or trout or their bi-products from China, North Korea or Taiwan;
 - goods restricted irrespective of country of origin or shipment, such as nuclear related products, weapons or chemical weapons; and
 - certain goods requiring a prior confirmation or confirmation at the time of customs clearance, by submitting certain certificates from Ministry of Trade, Economy and Industry or other relevant authorities, such as certain vaccines imported for clinical trial study, or cultural heritage assets.

FEFTA also restricts the assignment of patents, trade marks and other industrial property rights by requiring certain filings through the Bank of Japan with the Ministry and Finance and other ministries with jurisdiction over the relevant industry.

17. What import duties apply to commercial goods and services?

Customs duties and national and local consumption taxes are payable on imported commercial goods and services provided in Japan.

Goods imported to the customs zone in Japan can only be moved from the customs zone after completing an import declaration. The consignee under an invoice must pay customs duties before removing goods from the customs area. These duties are determined according to the value or volume specified in the import declaration, depending on the nature of the goods. A customs tariff schedule providing for the taxation rate for each imported item is set out in the Customs Tariff Law and other relevant regulation. Approximately one-third of the items listed in the schedule are duty free. An advance ruling system is available

whereby importers may make written inquiries with customs authorities regarding certain importations.

General consumption taxes applicable to goods and services are calculated based on their value. Certain goods such as liquor, tobacco, volatile oils, petroleum, gas, and petroleum coal attract additional customs duties. See *Question 21*.

18. Are the safety regulations and standards applicable to commercial goods and services in your jurisdiction compatible with other standards that are recognised internationally?

In general, safety regulations and standards applicable to commercial goods and services in Japan are not more onerous than internationally recognised standards. Japan is a member of the World Trade Organisation and a signatory to the Agreement on Technical Barriers to Trade and the Agreement on the Application of Sanitary and Phytosanitary Measures. As a result, under these arrangements, Japan generally cannot establish prohibitive safety regulations and standards. However, regulations and standards that are more onerous than international standards may exist for specific products or industries. Importers of commercial products to Japan should consult with the relevant authority with jurisdiction over such products or industries to confirm the applicable safety regulations.

STRUCTURING AND TAX

19. How is foreign investment into your jurisdiction typically structured? What forms of legal vehicle are attractive to foreign investors?

Limited liability stock company (*kabushiki kaisha*)

The most common corporate structure in Japan is the *kabushiki kaisha* (KK), a limited liability stock company, with internal organisation and operation prescribed under the Companies Act. A KK must have at least one shareholder and one director. However, it is common for a KK to have a board of directors consisting of three or more directors. A KK requires at least one representative director, who must be resident in Japan.

When a foreign investor establishes a KK as its Japanese subsidiary, corporation tax is payable on the income of the KK in Japan. Dividends to shareholders are also generally taxable. Therefore, there are fewer tax benefits available to a KK compared to other structures. Certain measures can be taken to avoid double taxation, such as excluding dividends from the taxable income of the shareholder if the shareholder is a Japanese entity. In addition, exemptions or reductions can be available under tax treaties if the shareholder is a foreign corporation or not resident in Japan.

Limited liability company (*godo kaisha*)

A *godo kaisha* (GK) is also established under the Companies Act, and like a KK is a limited liability company in which the members are liable only to the extent of their investment into the GK's capital. The incorporation procedures are simpler in comparison to a KK, and a GK has more flexible internal control under its articles of incorporation. At least one representative member of a GK, or if such representative member is a foreign corporation, at least one executive manager of such member corporation, must be resident in Japan.

Tax treatment for a GK is generally the same as for a KK, in that net income earned by the GK and profit distributions to its members are taxed.

A GK is often used with a profit sharing agreement investment scheme (*tokumei kumiai*) (TK). This structure is referred to as a GK/TK scheme. By entering into a TK agreement and forming a TK

in which a GK is a business operator, the profits to be distributed to members under the TK agreement can be deducted from the taxable income of the GK, acting as a pass-through to its members.

Profits distributed to non-resident members or foreign corporations are treated differently depending on whether the member has a permanent establishment in Japan. If it does not have a permanent establishment in Japan, a 20% withholding income tax would be payable on the distribution, unless otherwise provided for in an applicable tax treaty.

Branch

A branch does not have an independent judicial personality and conducts business in Japan pursuant to decisions made at the headquarters located outside of Japan. This is the simplest structure in which to conduct business in Japan because it is not necessary to establish articles of incorporation or to comply with statutes concerning internal procedures and other internal control issues. However, because it conducts business in Japan, certain matters concerning the branch must be registered with the relevant legal affairs bureau and made public, under the Companies Act. A branch must have at least one representative who is resident in Japan.

Currently, only a branch's domestic-source income is taxable. However, the tax treatments of income generated by permanent establishments, including a branch of a foreign corporation, are expected to be changed from April 2016 based on the Authorised OECD Approach (AOA) under Article 7 of the Model Tax Convention on Income and on Capital. After the change, income earned by a permanent establishment as a separate and independent entity from its headquarters will be taxed separately from other income generated by the foreign company in Japan, subject to adjustments for intercompany transactions and cost allocations. The AOA is considered to be a means to avoid double tax or double non-taxation. Advice from local tax specialist should be sought in anticipation of such changes.

Representative office

A representative office is the simplest structure for establishing a presence in Japan. It can be used for performing market research, promotion and advertisement or other preparatory activities prior to the full launching of a business in Japan. Business beyond such preparatory activities is not permitted. Filing with the relevant authority may be required depending on the industry or business. For example, notification to the Financial Services Agency is required with respect to banking business. However, registration with the local legal affairs bureau, which is required in relation to other structures, is not required. Generally, a representative office is not regarded as a permanent office and therefore would not be subject to corporation taxes. However, the representative individual's domestic-source income, including the income earned as representative, would be taxed in Japan.

20. What are the circumstances under which a business becomes liable to pay tax in your jurisdiction?

An incorporated entity in Japan is required to pay tax in Japan according to its worldwide income. Branches of foreign corporations are taxed on domestic-source income only. The manner of imposition of tax, such as comprehensive taxation or separate taxation at source, varies depending on whether the foreign corporation has a permanent establishment in Japan, as defined with reference to Article 7 of the Model Tax Convention on Income and on Capital. If a foreign corporation has established a branch office or other establishment to conduct business within Japan, that corporation would be comprehensively taxed on all the domestic-source income. However, if its presence in Japan is restricted to an individual agent or representative, for instance an individual who is authorised to execute contracts in Japan on behalf of the corporation, the corporation's income would be taxed

either by comprehensive taxation or separate taxation at source, depending on the nature of the income.

21. What are the main business tax rates?

Income generated from a corporation's business activities are liable to:

- Corporate tax.
- Corporate inhabitant tax.
- Business tax.
- Special local corporation tax.

Tax rates depend upon the corporate structure and amount of income.

As of December 2014, the corporate tax rate for a corporation such as a KK or GK is 25.5% of annual income exceeding JPY8 million, with an additional 2.55% as a special reconstruction income tax. In addition, the company is liable for corporate inhabitant tax at the rate of 4.41% (if the corporation is located in Tokyo), business tax at the rate of 5.3%, and special local corporation tax at the rate of 4.29%. In addition to corporate tax, consumption tax is payable on domestic transactions or transactions concerning the importation of goods or services. General consumption tax consists of national tax and local tax, with an aggregate tax rate of 8%. Tax returns must be filed with respect to payment of corporation tax and consumption tax.

Stamp duties are payable for documents satisfying certain conditions, for example:

- Land sale and purchase agreements.
- Service agreements.
- Articles of incorporation.

The amount of duty payable depends on a classification of the relevant documents and the contract amount under such documents. Stamp duties can be paid by purchasing revenue stamps. Failure to pay stamp duties does not render a document unenforceable or inadmissible. However, penalties are applicable for non-payment.

22. What is the tax treatment in your jurisdiction of profits from an investee company remitted outside your jurisdiction by an investor?

When a corporation such as a KK or GK pays retained income after tax to a foreign parent corporation as a distribution of profits, the dividend is generally also taxable in Japan. The dividend would be regarded as a payment of domestic-source income subject to tax withholding in Japan. At the time of such payment to a foreign parent corporation or non-resident shareholder, the resident corporation must deduct income tax and special reconstruction income tax and pay these taxes on behalf of the foreign corporation or non-resident. If the remittance is not made within one year of the date of determination of such a dividend, it is treated for tax purposes as having been paid one year from its declaration.

Deduction at source applies where a non-resident member of a partnership receives a distribution of profits under a partnership agreement. Payment is treated as having been made on that day which is two months from the end of the calculation period, even if the payment was not actually made.

For a branch of a foreign corporation, no taxes are generally payable when transferring funds to its foreign headquarters, where such funds come from profits which have been already subject to

corporation taxes as domestic-source income, and therefore no withholding tax is payable on the remittance.

If there is a tax treaty between the country of the non-resident and Japan, withholding income taxes on a dividend can be exempted or reduced. However, the non-resident would need to make a filing, through the payer, with the relevant local tax office.

23. What transfer pricing and/or thin capitalisation restrictions may apply to investments into your jurisdiction from elsewhere?

Transfer pricing rules are applicable in Japan. The calculation method for transfers between affiliated companies is in line with the OECD Transfer Pricing Guidelines, and in addition to the three basic methods of the comparable uncontrolled price method, resale price method and cost plus method. The transactional net margin method and profit split method may also be used. It is possible to obtain a prior confirmation from the relevant tax authority to the effect that a particular inter-company transaction is made at a certain price.

Thin capitalisation restrictions are also applicable. The restriction in Japan is applicable if the amount of loans which a domestic corporation takes out from a foreign controlling shareholder is more than triple its equity capital, or if the aggregate amount of the debts owed by the domestic corporation is more than triple its equity capital. If so, the interest paid by the domestic corporation to its foreign controlling shareholder for the amount exceeding triple its equity capital cannot be deducted from taxable income as an expense. A permissible ratio of loan to equity capital may be determined reasonably by comparison to domestic corporations engaging in similar industries, if certain conditions are satisfied.

INCENTIVES

24. What tax incentive or other schemes exist to encourage foreign investment?

Projects promoting FDI, site location and regional development in Japan

This programme is intended to sustain and strengthen existing high value-added business sites, and support the establishment of new high value-added sites in Japan by global companies operating internationally, for example, establishing regional headquarters or research and development (R&D) sites. So far, around ten companies with headquarters in the US or EU have availed themselves of the benefits.

Projects for relocation or consolidation of existing sites in Japan are not eligible for the subsidy, unless it involves the designation of a new role as a regional headquarters or R&D site. Projects must satisfy certain requirements, such as with respect to business contingency plans. Eligible projects can have certain expenses such as survey design costs, facility costs, equipment costs, and facility rental charges subsidised by the Japanese government by up to a half, subject to a maximum of JPY350 million, depending on the size of the business at the sites.

Comprehensive Special Zones for International Competitiveness

The Japanese government has designated special zones throughout Japan in order to strengthen regional development and international competitiveness.

As of December 2014, seven special zones have been designated as follows:

- Hokkaido Food Complex (Hokkaido).
- Tsukuba (Ibaraki Prefecture).

- Asia Head Quarter Tokyo (Tokyo).
- Life Innovation in Keihin Coastal Areas (Kanagawa Prefecture).
- Special Zone to Create Asia's No.1 Aerospace Industrial Cluster (Nagano Prefecture).
- Kansai Innovation (Kyoto Prefecture).
- Green Asia (Fukuoka Prefecture).

Certain tax benefits are available in such special zones, for example, special depreciation allowances or other tax deductions for investments in machines or buildings used for businesses coinciding with the strategy of the special zone.

The Asia Head Quarter Tokyo Special Zone covers business districts in the metropolitan area, and aims to invite more than 500 foreign companies, including 50 foreign companies establishing Asian regional headquarters or R&D sites. The initiative aims to attract industries including telecommunications, medical and chemical, electronics and sensitive equipment, finance and securities, and content and creative industries, through deregulation and tax benefits.

INVESTMENT GUARANTEES

25. What legal guarantees exist against expropriation and/or provide for appropriate compensation? What is your government's track record in this regard?

The Constitution of Japan provides that the right to own or to hold property is inviolable, that property rights must be defined by law in conformity with the public welfare and that private property can be expropriated for public use where there is just compensation to the holder of such rights. Various laws provide, in compliance with the requirement under the Constitution, for compulsory acquisition of property by the government or business operators, as authorised by the government in specific circumstances. For example, under the Compulsory Purchase of Land Act, real estate and rights concerning real estate may be used or acquired for projects of public interest such as roads, railways, electricity, water and social welfare, by the business operator of such projects. The authorised business operator must compensate the owners of real estate or other compulsorily acquired rights in an appropriate amount. An appropriate amount of compensation is generally considered to be based on the amount by which the owner would be able to acquire equivalent property in the same vicinity. For the last few years, approximately 20 to 30 projects have been approved to include compulsory acquisition under the Act. Other statutes providing for the expropriation include the Mining Act, Forest Act, and Telecommunications Business Act.

26. Are there any issues in relation to the enforcement of intellectual property rights?

Patent, copyright, trade mark and design rights are the main categories of intellectual property rights protected by law in Japan. Utility model rights and plant breeders' rights are protected under these categories.

Patent, trade mark and design rights are protected on registration. When a patent is infringed, remedies available under the Patent Act or Civil Code include:

- Injunctions.
- Damage compensation.
- Measures to restore credibility (such as the publication of an apology).
- Return of unjust enrichment.

- Compensation of royalties payable due to infringement made between patent application publication and registration.

Criminal sanctions may also be imposed.

In addition to remedies available under the intellectual property laws, remedies under the Unfair Competition Prevention Act may also be available. This legislation regulates actions constituting unfair competition, and may protect intellectual property rights for which registration has not been made. For example, the use of an identifying mark identical or similar to a trade mark well known to consumers, which results in confusion among consumers, may be regarded as a violation of the Unfair Competition Prevention Act, even if the trade mark is not registered. Remedies available under the Unfair Competition Prevention Act include:

- Injunctions.
- Compensation for damages.
- Measures to restore credibility.

Criminal sanctions may also be available.

Another relevant issue regarding intellectual property rights is the regulation of parallel imports, that is, imports made by parties other than authorised distributors. These unauthorised imports generally infringe intellectual property rights, but the courts have interpreted the law so that certain parallel imports are permitted. With respect to products protected by trade mark, parallel imports may be allowed if the following criteria apply:

- The products are the genuine products to which the trade mark is legally attached by the authorised trademark holder.
- The holder of the trade mark in a foreign country is the same as, or substantially the same as the holder of the trade mark in Japan.
- The products imported in parallel are of a quality equivalent to the products of the trade mark holder distributing the products in Japan.

In seeking remedies with respect to intellectual property rights, issues with respect to the court procedures should be considered (*see Question 27*).

27. Are there any issues in relation to the gaining and enforcement of judgments and/or arbitral awards?

Foreign investors receive the same treatment as domestic parties in Japanese courts. However, a person with no presence in Japan may be required to deposit a surety for the costs of the action. Proceedings in Japanese courts are conducted in Japanese, and court documents and evidence must be produced in Japanese or accompanied by a Japanese translation.

Some other obstacles faced by foreign nationals participating in court proceedings in Japan include the following:

- Japanese court proceedings are considered to be lengthy and time consuming compared to proceedings in some other developed countries. The Supreme Court of Japan published a survey report in 2013 that the average time from the first hearing date to obtaining judgment or settlement in the first trials of civil litigation cases (excluding claims for return of excess payment of interests on borrowing) is 8.9 months. However, this depends on the complexity of the case and it is not uncommon to take 18 months or longer, and in some cases, several or more years, to obtain a judgment. It is common for litigation in Japanese courts to be concluded by settlement before a final determination.

- Japanese courts do not have a process of discovery or the concept of privilege, although the court may order a party to disclose certain documents at the other party's request. However, as it would be generally required to specify the requested documents, parties must first collect evidence before prosecuting or defending a claim on their own.

- Under the Code of Civil Procedures, an unsuccessful party may pay the costs of the action for the successful party. However, an award of costs in Japan does not include attorney fees. The Act on Costs of Civil Procedure contains certain items that can be recovered, which include the costs of the fees payable to the court at the time of the petition, the costs of witnesses, appraisers and interpreters (including travel expenses, daily pay, and accommodation costs), and the costs to prepare and mail court documents.

Judgments obtained in foreign courts are generally enforceable in Japanese courts, subject to satisfaction of terms required by the Code of Civil Procedures, including, for example, reciprocal treatment (meaning the country of the foreign court allowing enforcement of judgments rendered by Japanese courts under similar conditions) and proper service to a Japanese defendant of properly translated documents.

Arbitration awards obtained abroad are enforceable in Japan under the New York Convention on Recognition and Enforcement of Foreign Arbitration Awards if the arbitration award is rendered in a member country. Court procedures to enforce such arbitration awards may take several months.

Foreign investors can avoid difficulties such as the language issues or delays discussed above by using arbitration through the Japan Commercial Arbitration Association (JCAA). Arbitration can be conducted in any language agreed by the parties. Under the JCAA rules, the arbitration panel can make an award of costs, including attorney's fees, in favour of the successful party. Discovery procedures are not available under the JCAA rules, and the costs and fees payable to the arbitration organisation may sometimes be much more than the costs and fees payable when the case is brought to court.

Parties may also elect to have disputes resolved at a forum of international arbitration such as the International Chamber of Commerce or the International Centre for Dispute Resolution – American Arbitration Association, with the venue in Japan. The Code of Civil Procedure applies in enforcing the arbitral award in courts in Japan.

RECENT DEVELOPMENTS AND PROPOSALS FOR REFORM

28. Have there been any significant recent or proposed legal developments affecting investors?

The Act on Special Measures for Promotion of Research and Development Business, etc. by Specified Multinational Enterprises

This Act came into effect on 1 November 2012, with the purpose of inviting foreign companies to establish research and development (R&D) sites or regional headquarters in Japan (*see Question 24*).

The following support is available for companies that satisfy certain conditions with respect to incorporating affiliates in Japan to conduct R&D, or for the control of their business in Japan, if the ministry with jurisdiction over the relevant industry or business certifies the business plan:

- Special treatment with respect to corporate tax and income tax. This includes a deduction of 20% of the income generated by the R&D businesses from taxable income for each business year ending within five years from certification. Depending on the geographic area, reduction in local taxes (corporate inhabitant

tax and business tax) may also be available. Therefore, a significant reduction in corporate tax is possible. Special treatment for income tax includes, for the grant of share options by a foreign parent, delay of taxation to the time of the sale of the relevant shares, for which the maximum tax rate would be 20%.

- Shortened periods for investment procedures in certain cases where a filing would be required under FEFTA.
- Equity financing support by the Small and Medium Business Investment & Consultation Co, Ltd.
- Reduction by half of patent examination fees and patent fees for patentable invention.
- Acceleration of patent application examinations and trial examinations for patent applications for the results of R&D conducted under the programme.
- Special treatment with respect to immigration procedures, such as fast-track issuance of Certificates of Eligibility.

Immigration procedures for highly-skilled foreign nationals

A points system for highly skilled foreign nationals was introduced in May 2012 (see *Question 9*). The following additional benefits are now available:

- Performing multiple activities is now permitted, and the applicant is not restricted to specific eligibility, as was previously the case.
- The eligibility period is five years without exception.
- Permanent residence can be applied for after only five years of residence, as opposed to ten years of residence as previously required, as well as preferential processes in relation to immigration procedures.
- Permission for spouse to work.
- Parents of such persons are permitted to accompany their children under certain conditions.
- Domestic helpers are permitted to accompany their employers under certain conditions.

Special casino zone

Gambling is currently prohibited under Japanese law except for certain gambling activities that are operated by government-affiliated corporations or local governments (for example, horseracing and motorboat racing). The national government is currently considering legislation to allow privately operated casinos to operate in Japan. As there are no experienced operators in Japan, it is expected that foreign investors will participate. Casinos will operate within an integrated resort facility consisting of hotels, conference rooms, recreation facilities and exhibition facilities. It is expected that such casinos will only be permitted in special zones, and that the local government with jurisdiction over the special zone would choose private business operators permitted by the relevant authority to establish and operate the integrated resort

facility. It is currently expected that a bill to establish the special casino zones will be submitted to the Diet in the spring of 2015. The government intends to have such integrated resorts operating by 2020 when Tokyo will host the Olympic Games.

29. Are there any planned or on-going treaty negotiations or political developments that could have an impact on your jurisdiction's bilateral relationships with other nations and/or other economic, customs or monetary unions, free-trade areas or markets?

Trans-Pacific Strategic Economic Partnership Agreement (TPP)

Japan is currently negotiating the TPP, a comprehensive free trade agreement by and among 12 countries around the Pacific Ocean, comprising New Zealand, Singapore, Chile, Brunei, the US, Australia, Peru, Vietnam, Malaysia, Mexico, Canada and Japan. The subject of negotiations include:

- Tariff removal.
- Trade facilitation (in relation to establishing the rules on sanitation and plant quarantine measures establishing standards specifications and compatibility, and simplifying custom procedures).
- Service liberalisation.
- National treatment of government procurement.
- Co-operation in relation to competition and intellectual property rights issues.

A co-operation framework in strategic areas such as technical innovation and R&D.

Regional Comprehensive Economic Partnership (RCEP)

RCEP is a free trade arrangement being negotiated as between ten ASEAN countries, (comprising Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, and Vietnam) as well as Japan, PRC, South Korea, Australia, New Zealand and India. The arrangement aims to cover trade in goods and services, direct investment, co-operation in the fields of economics and technology, intellectual property rights, competition law and dispute resolution.

Free Trade Area of the Asia-Pacific (FTAAP)

FTAAP is a planned comprehensive free trade arrangement among the 21 countries and territories comprising the Asia-Pacific Economy Cooperation (APEC). The proposal has only recently been put forward by APEC and formal negotiations have not commenced. It is expected that such comprehensive agreement would address trade facilitation including the areas of investment, services, e-commerce, and supply chain connectivity such as international logistics facilitation.

For bilateral relationships, please see *Question 7*.

MAIN INVESTMENT ORGANISATIONS

Japan External Trade Organisation (*Nihon Boeki Shinko Kiko*) (JETRO)

JETRO engages in promoting foreign direct investment into Japan, promoting trade and business between Japan and the rest of the world, assisting business expansion of developing countries, contributing to trade policies and economic partnership, researching developing economies and providing support and information on overseas business.

W www.jetro.go.jp

Manufactured Imports and Investment Promotion Organisation (*Ippan-zaidan Hojin Tainichi Boeki Toshi Koryu Sokushin Kyokai*) (MIPRO)

MIPRO engages in the business of supporting investments into Japan, as well supporting importation businesses, collection, provision and consultation for intellectual property rights, product safety and welfare, and introducing developing countries' products into Japan.

W www.mipro.or.jp/english

ONLINE RESOURCES

Invest Japan

W www.invest-japan.go.jp/en_index.html

Description. The Invest Japan website is operated by Cabinet Office. It provides links to the websites of the offices of Invest Japan held at the ministries and other governmental offices.

Japanese Law Translation

W www.japaneselawtranslation.go.jp/?re=02

Description. This Japanese Law Translation database is operated by the Ministry of Justice and provides unofficial English translations of Japanese laws and regulations. Please note that it provides only tentative translations for some laws and regulations, and some of the translations it provides are out-of-date, as they are not necessarily updated after amendments to the relevant laws and regulations.

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Japan, Lawyer (*bengoshi*)

Areas of practice. Mergers and acquisitions; investment funds.

Recent transactions

- Acting for US foreign exchange firms in acquisition of Japanese companies and developing regulated businesses in Japan.
- Advising UK and US major banks on Japanese laws and regulations applying to various Japan-related financial activities conducted directly or through Japan subsidiaries.
- Advising a US major investment bank on collateralised reinsurance transactions with major Japanese insurance companies.
- Acting for a number of foreign institutional investors (including sovereign and pension funds) on litigations in relation to their investment into a Japanese listed company.

Publications

- Japan – changes in regulation following the AIJ scandal, Euromoney Yearbooks - Global Asset Management & Servicing Review 2013/14, Euromoney Institutional Investor PLC (2013).
- Aiming at diversity, IFLR JULY/AUGUST 2012, IFLR (2012) [Co-author].
- Japan - Changes in Regulation, Euromoney Yearbooks - Global Asset Management & Servicing Review 2012/13, Euromoney Institutional Investor PLC (2012).

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Professional qualifications.

Japan, Lawyer (*bengoshi*), Certified Public Accountant

Areas of practice. Securities litigation; corporate; renewable energy; disclosure policies; risk management.

Recent transactions

- Advising a foreign major PV developers for a largest-scale farming type solar power project in Japan.
- Investigation of alleged irregularities at the Japan office of a foreign corporation.
- Acting for a number of institutional investors on litigations in relation to a claim for damages based on annual securities report containing false statements.
- Assisting with improving group business management of a major securities company group, risk management of overseas subsidiaries.

Languages. Japanese and English.

Publications

- "Industry-Classified Accounting: Securities Business", *Daiichi-Hoki* (2012).

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Professional qualifications.

Japan, Lawyer (*bengoshi*)

Areas of practice. Mergers and acquisitions; corporate; labour; dispute resolution.

Recent transactions

- Acting for a US semiconductor manufacturer in its acquisition of a business of a Japanese semiconductor designer and manufacturer.
- Acting for a US medical equipment manufacturer in terminating a Japanese exclusive distributorship which was, in substance, an acquisition of a material part of the distributor's business.

Languages. Japanese and English.

Publications.

- *"Lay-offs and Age Discrimination Issues for Japanese Companies Doing Business in the U.S.", Come to America Vol.25, U.S. Japan Publication N.Y., Inc. (2011).*
- *"Overview of U.S. Bankruptcy Law and Procedure: Dealing with Customers in These Troubled Economic Times", Come to America Vol. 24, U.S. Japan Publication N.Y., Inc. (2010).*