

# Japan tax alert

Ernst & Young Tax Co.

## 2025 Japan tax reform outline (Overview)

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The fiscal year 2025 tax reform outline was released on 20 December 2024. In this alert, we provide an overview of the major reforms and revised provisions contained in the outline. Please note that the contents of the reform outline may be subject to revisions during discussions among the ruling and opposition parties, or throughout deliberations regarding the reform bill in the Diet.

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# Corporate taxation

## 1. Special measures for small and medium enterprise (SMEs) corporate tax reduction

This special measure will be revised as follows and extended by 2 years.

- ▶ For fiscal years with annual taxable income in excess of JPY1 billion, the current special tax rate of 15% applicable to annual taxable income up to JPY8 million will be increased to 17%.
- ▶ Group companies under the group relief system will be excluded from the scope of this measure.

## 2. Taxation related to SMEs

- ▶ The SME investment incentive tax rules will be revised and extended by 2 years.
- ▶ The SME business enhancement tax rules will be revised and extended by 2 years. Additionally, subject to future revisions to relevant laws and regulations, measures will be implemented for SMEs aiming to exceed JPY10 billion in revenue. Buildings will also be added as eligible assets under relevant rules.
- ▶ The special measure for the taxable base used for fixed asset tax related to SME capital investments will be extended by 2 years.

## 3. Taxation related to corporate reorganizations

- ▶ The calculation method for adjustment accounts in relation to assets transferred as result of a non-qualified merger will be clarified.
- ▶ In order to facilitate tax qualified spin-offs of wholly-owned subsidiaries under the group relief system, necessary measures will be implemented in relation to the calculation of distribution ratios.

## 4. Others

- ▶ Necessary measures will be implemented to accommodate the revisions to the accounting standards for lease transactions.
- ▶ Tax incentives to encourage investment in the future of regional areas will be extended by 3 years.
- ▶ The measures for hometown tax for businesses will be extended by 3 years.
- ▶ Tax incentives for 5G implementation and the digital transformation investment promotion tax incentive will be abolished.

## International taxation

### 1. Global minimum taxation

- ▶ Legislation on the Undertaxed Profits Rule (UTPR) and Qualified Domestic Minimum Top-up Tax (QDMTT) will be enacted. To afford affected companies ample time to prepare for new administrative procedures, the legislation will be applicable to fiscal years beginning on or after 1 April 2026.
- ▶ Necessary revisions will be implemented to clarify the taxation system, in light of the details published in the OECD Guidance.

### 2. Japanese Controlled Foreign Company ("JFC") rules

- ▶ The amount equivalent to the CFC taxable income of a foreign affiliated company will be included in the parent company's taxable income in the fiscal year of the parent company that includes the last day of the fourth month (currently, the second month) following the end of the fiscal year of the foreign affiliated company.
- ▶ This revision will apply to the CFC taxable income of a foreign affiliated company (limited to the CFC taxable income relating to its fiscal year ending on or after 1 February 2025) relating to the parent company's fiscal year starting on or after 1 April 2025. Transitional measures will be implemented to enable early application of this revision.

## Individual income taxation and asset taxation

### 1. Revision of individual income taxation

- ▶ The basic deduction and minimum employment income deduction for individual income tax (national taxes) will be increased to JPY580 thousand (currently JPY480 thousand) and JPY650 thousand (currently JPY550 thousand), respectively. The annual income threshold for taxation will be brought up from JPY1.03 million to JPY1.23 million.
- ▶ The maximum qualifying income of college-aged children under the specified deduction for dependents will be raised to JPY1.5 million (currently JPY1.03 million). In addition, the reduction of dependent deductions for high-school aged children will be deferred.
- ▶ The above revisions will apply from 2025.

### 2. Others

- ▶ The additional borrowing limit for the housing loan tax credit aimed at supporting young married couples and households with children will be extended into 2025.
- ▶ Revisions will be implemented to enhance the convenience of NISA. The maximum monthly contribution for the individual-type defined contribution pension plan (iDeCo) will be increased.
- ▶ Revisions will be made in regard to calculations of individual income in cases where beneficiaries are newly decided for a trust subject to corporate taxation without beneficiaries.
- ▶ The period for reinvestment will be extended under the angel investor tax rules.
- ▶ Revisions will be made to the requirements for executive appointment under the business succession tax rules.
- ▶ The applicable period for the gift taxes exemption measures for lump-sum gifts of marriage and child-rearing funds will be extended by 2 years.

## Consumption taxation

### Revision of consumption tax exemption rules for foreign tourists

- ▶ To eliminate the misuse of these exemption rules and ensure duty-free stores are not forced to bear the burden of combating such misuse, and in light of the plan outlined in the 2024 tax reform, these rules will be revised so that sales are approved as tax-free upon confirmation that a foreign tourist has taken the purchased goods outside of Japan. This revision will change the current exemption rules to a “refund system” where tax-free shops reimburse the equivalent amount of consumption tax to foreign travelers once it has been confirmed the purchased goods have left the country.
- ▶ This revision will be applied to tax-free eligible transactions on or after 1 November 2026.

## Tax rules and measures for national defense build-up

### 1. Creation of defense special tax (tentative)

- ▶ A new surtax of 4% will be imposed on the standard corporate tax amount (i.e. taxable base) of corporations. The standard corporate tax amount for purposes of this surtax will be determined by deducting JPY5 million (the basic deduction amount) from the corporate tax amount.
- ▶ This taxation will apply to fiscal years beginning on or after 1 April 2026.

### 2. Others

- ▶ Tax increases on tobacco will be put in place accordingly, starting in April 2026.
- ▶ The determination of the timing of planned increases to individual income taxes will be postponed.

# | Tax administration

## 1. Revision of the electronic book preservation act (e-retention) rules

- ▶ Electronic data that satisfies certain requirements will be excluded from the scope of aggravated measures for heavy additional tax in relation to electronic books.
- ▶ Requirements for the application of special deductions for blue return filings (JPY650 thousand) will be revised.

## 2. Enhanced convenience of e-Tax

- ▶ A system to electronically submit copies via e-LTAX will be implemented for local taxes.

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