

Application for Approval to File a Blue Tax Return			
To the Head of the Tax Office	Address and telephone number of residence, office, etc, where tax is paid		
	Addresses and telephone numbers of other residences, offices, etc		
Date:	Name:	Date of birth:	
	Occupation:	Business name:	
Year for which approval to file a blue return is requested			
1. Name and location of office assets or income-producing assets			
	Name:	Location:	
	Name:	Location:	
2. Type of income: Business * Real property * Forestry			
3. Has a previous approval to file a blue tax return request been cancelled or withdrawn?			
	(1) Yes (cancelled or withdrawn) date	(2) No	
4. If a new business has been started on or after 16 January of this year, the date that business was started			
5. Was a business inherited?			
6. Other reference items			
	(1) Bookkeeping system (circle the method used for the blue return purposes)		
	Double-entry bookkeeping	Simplified bookkeeping system	Other ()
	(2) Reference items (circle the books of account used in connection with the blue tax return)		
	Cash receipts and disbursements	Sales	Purchases
	Expenses	Fixed assets	Deposits received and paid
	Receivables	Debts	Transfer slip
	General ledger	Journal	Cash basis simple account book
	Receipts slips	Payment slips	Others
	(3) Others		
Name and telephone number of licensed tax accountant		For use of the tax office	

Law: Art 4-5(2), Art 4-5(2)(iv), Art 4-5(2)(v), Art 122(1), Art 122(2), Art 148 and Art 149 of the *Corporation Tax Law*; Art 143, Art 144 and Art 230 of the *Income Tax Law*

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INTRODUCTION

[¶3-100] Introduction

This chapter describes the major taxes applicable to individuals who are residents of Japan, with a primary focus on the Income Tax. Application of the Income Tax to corporations is discussed in Chapter 4 (Corporation Tax) and income taxation of non-residents of Japan is discussed in Chapter 9 (Non-residents and Foreign Corporations).

THE INCOME TAX (*SHOTOKUZEI* — 所得税)[¶3-200] The Income Tax (*Shotokuzei* — 所得税)

The Income Tax is primarily a direct tax on the income of individuals who are residents of Japan and on some kinds of Japanese source income of non-residents. However, the Income Tax is also used as a means of collecting tax by withholding on certain types of income of domestic and foreign corporations. A corporation which files a final (annual) Corporation Tax return in Japan may take a credit for Income Tax paid (CTL Art 68). The following table summarises the income subject to Income Tax for the four basic groups of taxpayers subject to the tax (ITL Art 7(1)).

Table 1: Income subject to Income Tax

Taxpayer	Basis of taxation
Individual resident of Japan (other than a non-permanent resident)	All income (ITL Art 7(1)(i)).
Individual non-resident or non-permanent resident of Japan	Enumerated types of domestic source income (ITL Art 7(1)(ii), Art 7(1)(iii)) (see Chapter 2). Non-permanent residents are also subject to Income Tax on other income paid in Japan or remitted from outside Japan.
Japanese domestic corporation	Interest, dividends, compensation benefits, rewards, fees and prizes paid in Japan and described in ITL Art 174 (ITL Art 7(1)(iv)).
Foreign corporation	Japanese source income described in ITL Art 161(1)(ii) through (vii), and (ix) through (xii) (ITL Art 7(1)(v)).

Law: Art 68 of the *Corporation Tax Law*; Art 7(1), Art 7(1)(i), Art 7(1)(ii), Art 7(1)(iii), Art 7(1)(iv), Art 7(1)(v), Art 161(1)(ii) through (vii), Art 161(1)(ix) through (xii) and Art 174 of the *Income Tax Law*

[¶3-210] Income taxation of permanent resident individuals

Individuals who are permanent residents of Japan are subject to the Income Tax according to three different systems:

- aggregate assessment taxation (*sogokazei*)
- separate assessment taxation (*shinkoku bunrikazei*), and
- separate withholding taxation (*gensen bunrikazei*).

Aggregate assessment taxation is a comprehensive self-assessment income tax system under which the taxpayer files a final tax return reporting income for the calendar year. Separate assessment taxation allows taxpayers to report certain specified types of income, such as gains from the transfer or sale of securities not subject to the separate withholding taxation election, on the tax return separately from income subject to aggregate assessment taxation and at flat rates of Income Tax (STML Art 37-10). The separate withholding taxation system provides for Income and Inhabitants Tax liabilities to be satisfied completely through withholding, eliminating the need for the income to be reported on a tax return.

Law: Art 37-10 of the *Special Taxation Measures Law*

¶3-220] Aggregate assessment income taxation (*Shinkoku Shotokuzei* — 申告所得税)

Under the aggregate assessment income taxation system, a taxpayer is taxed on a net basis, after allowable deductions, on his/her ordinary income amount (*soshotoku kingaku*) (ITL Art 22(2)), retirement income amount (*taishoku shotoku kingaku*) (ITL Art 30) and forestry income amount (*sanrin shotoku kingaku*) (ITL Art 32). Tax is computed separately on each of these net amounts (ITL Art 22(1), Art 89), but losses arising from real property, business, forestry or transfers may be used to offset income in other categories (ITL Art 69(1)) according to ordering rules provided in the regulations (ITL-EO Art 198).

- The ordinary income amount is reported on a final Income Tax return for the calendar year (*shotokuzei no kakutei shinkokusho*).
- The tax liability for retirement income is satisfied through withholding so retirement income is usually not reported on a tax return unless there is an applicable loss offset against retirement income from other categories of income.
- Forestry income is reported on the tax return separately from other income and tax is computed using a special averaging calculation.

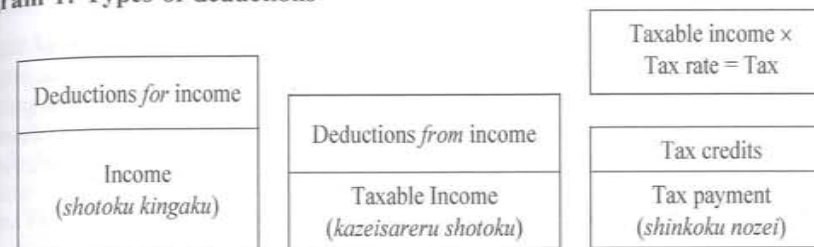
Law: Art 22(1), Art 22(2), Art 30, Art 32, Art 69(1) and Art 89 of the *Income Tax Law*; Art 198 of the *Income Tax Law Enforcement Order*

¶3-225] Deductions (*Kojo* — 控除)

For calculating Income Tax, three different types of deductions are allowed:

- Deductions for income (*shunyu kara sashihikareru kingaku*)
- Deductions from income (*shotoku kara sashihikareru kingaku*)
- Deductions from tax — tax credits (*zeikin kara sashihikareru kingaku*).

Diagram 1: Types of deductions



¶3-230] Ordinary income (*Soshotoku Kingaku* — 総所得金額)

There are eight categories of ordinary income (ITL Art 22):

- (1) Interest income other than interest subject to separate withholding taxation (STML Art 3)
- (2) Dividends (*haito shotoku*) other than dividends subject to separate withholding taxation (STML Art 8-5, Art 8-6)
- (3) Business income (*jigyo shotoku*)
- (4) Lease income (*fudosan shotoku*)
- (5) Employment income (*kyuyo shotoku*)
- (6) Capital gains (*joto shotoku*)
- (7) Occasional income (*ichiji shotoku*)
- (8) Miscellaneous income (*zatsu shotoku*)

Child allowance (*kodomo teate* — 子ども手当)

Beginning 1 April 2010, a child allowance is provided to the guardian of a child 15 years of age or less. The child allowance statute provides that the allowance is exempt from all taxes (*2010 Law Concerning Provision of the Child Allowance*, Law No 19, 31 March 2010, Art 15 — 平成二十二年度等における子ども手当の支給に関する法律).

Law: Art 22 of the *Income Tax Law*; Art 3, Art 8-5 and Art 8-6 of the *Special Taxation Measures Law*; Art 15 of the *2010 Law Concerning Provision of the Child Allowance*

¶3-231] Interest income (*Rishi Shotoku* — 利子所得)

Interest income includes interest from savings accounts, bonds and distributions from joint operation trusts and bond investment trusts (ITL Art 23). Although interest income is included as ordinary income in the base for the aggregate assessment tax (ITL Art 22(2)(i)), interest is usually taxed under an exception to the general rule at a flat 20% (15% national and 5% local) rate when received under the separate withholding income rules rather than being included in ordinary income (ITL Art 181(1), Art 182(1)(i); STML Art 3(1); *Local Tax Law* (LTL) Art 71-6(1)). If interest is included in ordinary income, the amount included is the amount of interest before deducting any tax withheld.

Use of the inherited property	% of value included in the tax base
Property used by a family corporation (see ¶4-611) controlled (ie 50% stock ownership) directly or indirectly by the decedent where the heir is a director of the corporation on the due date of the return and the property is used in the business continuously from the start of succession to the due date of the return.	20
Other small-scale business or residential land.	50

Law: Art 69-4 of the *Special Taxation Measures Law*

¶6-620 Special rules for valuation of property used by specified businesses
(*Tokutei Jigyo Yo Shisan No Tokurei* — 特定事業用資産の特例)

If specified unlisted stocks are received by inheritance or bequest, the heir may elect to include only 90% of their value in the tax base for the Inheritance Tax. No more than two-thirds of the outstanding stock of a corporation, and not more than ¥300m of value, may qualify for this special treatment. Specified unlisted stocks are stocks not listed on a stock exchange that satisfy certain conditions, including the following (STML Art 69-4):

- The value of all the issued stock of the corporation must be less than ¥2 billion.
- The decedent and persons related to the decedent must have owned more than one-half of the stock of the corporation.
- The heir must be a relative of the decedent and a person described in *Corporation Tax Law* Art 2(1)(xv) as a director, auditor, trustee, etc, of the corporation.

Law: Art 2(1)(xv) of the *Corporation Tax Law*; Art 69-4 of the *Special Taxation Measures Law*

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INTRODUCTION

¶7-100 Introduction

In Japan, indirect taxes make up a little over 40% of national tax revenues, which is less than commonly seen in Europe, but considerably more than in the United States. At the local level, indirect taxes make up less than 20% of tax revenues in Japan.

Table 1: International comparison of composition of national revenue ratio of direct taxes to indirect taxes (figures for Japan are estimates for 2012 and final figures for 2009; figures for the other countries are based on OECD data for 2009)

Country	National	Local	Combined
Japan (2012)	57:43	85:15	69:31
Japan (2009)	57:43	86:14	71:29
US	92:8	59:41	75:25
UK	59:41	100:00	61:39
Germany	44:56	94:6	50:50
France	51:49	50:50	51:49

Source: Japan Ministry of Finance

Japanese indirect taxes are of three general kinds: *ad valorem* Consumption Tax, specific consumption taxes based on units and circulation taxes on transactions and acts.

Diagram 1: Types of Japanese indirect taxes



The *ad valorem* Consumption Tax accounts for over half of the indirect tax revenues in Japan.

Table 2: Composition of Japanese indirect tax revenues 2009–2010

Indirect tax	Indirect tax revenues (¥1m)		% of indirect tax revenues	
	2009	2010	2009	2010
Consumption Tax	9,807,541	10,033,311	54%	55%
Gasoline Tax	2,715,189	2,750,101	15%	15%
Liquor Tax	1,416,756	1,389,290	8%	8%
Stamp duty revenue	1,067,572	1,024,021	6%	6%
Tobacco Tax	822,383	907,671	5%	5%
Motor Vehicle Tonnage Tax	635,112	635,112	4%	4%
Customs duty	731,880	785,881	5%	4%
Other	916,572	947,499	5%	5%
Total indirect taxes	18,113,005	18,284,315	100%	100%

Although politically unpopular, indirect taxes are projected to become an increasingly important component of the Japanese tax system in the future due to a “hollowing out” of the tax base for the Income Tax as the population ages. Most of this increased burden is expected to be taken up by increases in the Consumption Tax rate. The Tax Commission, Japan’s tax policymaking panel, believes that an increase in the Consumption Tax rate from the current 5% to 20% will be needed to handle Japan’s fiscal needs.

THE CONSUMPTION TAX (SHOHIZEI — 消費税)

¶7-200 The Consumption Tax (Shohizei — 消費税)

The *Consumption Tax Law* was enacted on 30 December 1988, effective for transactions on or after 1 April 1989. The original rate of 3% was raised to 5% (4% national tax and 1% Local Consumption Tax, which is set at 25% of the national rate) in April 1997.

Table 3A: Consumption Tax rates from 1 April 1997 through 31 March 2014

Combined Consumption Tax rate:	5%
National rate:	4% (<i>Consumption Tax Law</i> Art 29)
Local rate:	25% of the national rate (1%) (<i>Local Tax Law</i> Art 72-82, 72-83)

Increase in the rate of Consumption Tax. As part of a comprehensive plan to strengthen the stability of the social security system, on 22 August 2012, legislation was enacted which includes a two-stage increase in the Consumption Tax (*Law to Partially Revise the Consumption Tax Law in Order to Secure Stable Resources for Social Security* — 社会保障の安定財源の確保等を図る税制の抜本的な改革を行うための消費税法の一部を改正する等の法律, Law No 68, 22 August 2012, effective 1 April 2014).

Table 3B: Consumption Tax rates from 1 April 2014 (Law No 68, 22 August 2012, Arts 2 and 3)

Effective dates	Combined Consumption Tax rate	National rate	Local rate
Beginning 1 April 2014	8%	6.3%	1.7%
Beginning 1 October 2015	10%	7.8%	2.2%

The two-stage increase in Consumption Tax rates beginning 1 April 2014 is conditioned on continuing favourable economic conditions. Implementation of the tax rate increases may be halted if warranted after taking into consideration economic indicators such as real and nominal rates of growth and price trends (Law No 68, 22 August 2012, Supplementary Provisions Art 18). A goal to achieve an average nominal and real economic growth of 3% and 2% during the period from 2011 through 2020 is incorporated in the tax increase legislation.

System of reduced rates (on necessities) (*keigen zeiritsu seido* — 軽減税率制度). The 2012 tax rate increase legislation does not contain any provision for lower Consumption Tax rates on daily necessities such as food. However, the Tax Commission’s 2013 Tax Reform Report (see ¶1-130) provides for consideration of a Consumption Tax rate reduction system for certain classes of taxable items when the Consumption Tax rate increases to 10% in October 2015.

Transitional rules. During the period that the 8% Consumption Tax rate is in effect, under the following transition rules the pre-change 5% rate will continue to apply (Law No 68, 22 August 2012, Supplementary Provisions Art 5). Similar measures are expected to apply retaining the 8% rate during a transition period when the 10% rate comes into effect.

Item covered by transitional rule	Details
Entrance fees to a race track, bicycle race track, art museum, amusement park, film or play or amounts received for passenger	Amounts received before 1 April 2014 for services rendered after that date
Electricity, gas, telephone, etc, utility costs	Amounts received for services contracted before 30 April 2014 under a contract continuously in effect before 1 April 2014
Construction contract concluded between 1 October 1996 and 30 September 2013	Amounts received for transfers of taxable materials after 1 April 2014 under preexisting contract
Lease contract concluded between 1 October 1996 and 30 September 2013	Amounts received under lease contract after 1 April 2014 under preexisting contract provided certain conditions are satisfied regarding definiteness of payments and changes in contract terms, etc
Labour contract concluded between 1 October 1996 and 30 September 2013	Amounts received under labour contract after 1 April 2014

- (1) the location of a permanent establishment in Japan (the main permanent establishment if more than one)
- (2) the location of real property from which income is derived in Japan, or
- (3) the Kojimachi Tax Office in Tokyo.

Law: Art 17, Art 74(1) and Art 145 of the *Corporation Tax Law*; Art 16 of the *Corporation Tax Law Enforcement Order*

CHAPTER 10

INTERNATIONAL DOUBLE TAX RELIEF

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INTRODUCTION

[¶10-100] Introduction

A permanent resident of Japan or a Japanese domestic corporation is subject to Japanese Income Tax or Corporation Tax on all income, regardless of whether the income is sourced in or outside Japan (ITL Art 7(1)(i), CTL Art 5). A non-permanent resident of Japan is subject to Japanese tax on Japanese source income and on other income which is paid in Japan or remitted from outside Japan (ITL Art 7(1)(ii)). For these taxpayers, income from outside Japan may be taxed in Japan (the home country) and also in the foreign country (the source country). Without provisions to mitigate international double taxation, the resulting tax burden could make it not economically feasible to engage in transnational economic activity.

Example 1 — International double taxation

A taxpayer is a resident of a country which taxes the worldwide income of its residents at an effective rate of 50%, but does not provide any mitigation of international taxation. The taxpayer derives all its income from sales in a neighbouring country which taxes income sourced within its borders at an effective rate of 50%. Because the home country does not provide relief from international double taxation, the taxpayer is subject to an effective tax rate of 100%.

If the home country allowed the taxpayer to deduct the foreign taxes as an expense, the taxpayer's effective rate would be 75%.

International double tax relief is provided to Japanese taxpayers by means of a foreign tax credit and through international tax treaties.

Law: Art 5 of the *Corporation Tax Law*; Art 7(1)(i) and Art 7(1)(ii) of the *Income Tax Law*

FOREIGN TAX CREDIT (*GAIKOKU ZEIGAKU NO KOJO* — 外国税額の控除)

[¶10-200] Foreign tax credit (*Gaikoku Zeigaku No Kojo* — 外国税額の控除)

A Japanese domestic corporation or resident may take a credit, subject to limits, against Corporation Tax or Income Tax for foreign taxes corresponding to those Japanese taxes that are incurred during the taxable year (ITL Art 95; CTL Art 69).

Deduction or credit

A Japanese domestic corporation or resident may elect to take a credit or deduction for foreign taxes incurred during the taxable year (ITL Art 46; CTL Art 41). If the credit is elected, no deduction is allowed for any creditable foreign taxes.

Timing of the foreign tax credit

The foreign tax credit is allowed for the taxable year of the Japanese taxpayer, which includes the day the obligation is incurred (which is the day the obligation to pay the foreign tax becomes definite) (CTL Art 69(1); CTL Basic Circular 16-3-5).

Law: Art 41, Art 69 and Art 69(1) of the *Corporation Tax Law*; Art 46 and Art 95 of the *Income Tax Law*

¶10-210 Creditable foreign taxes

A credit is allowed only for foreign taxes on income, including excess profits taxes, taxes on income or a part of income, but which are assessed based on receipts or similar amounts, and taxes on income which are collected based on receipts for the convenience of tax collection (CTL Art 69(1); CTL-EO Art 141(1)). Taxes on income which are assessed based on receipts are commonly found in oil-producing countries and countries with substantial agricultural exports. Withholding taxes on interest, dividends and royalties are examples of taxes on income which are collected based on receipts for the convenience of tax collection (CTL Basic Circular 16-3-4). Value added taxes and penalty taxes do not qualify for the credit.

Disallowed foreign taxes

Regulations provide that the following taxes will not be treated as foreign taxes for purposes of the Japanese foreign tax credit (CTL-EO Art 141(3)):

- If the taxpayer has the option to demand full or partial refund of the tax.
- If the taxpayer has the option to determine the period in which the time for payment can be deferred. If the tax paid exceeds the minimum rate available to the taxpayer, only the tax under the minimum rate is considered a foreign tax.

Law: Art 69(1) of the *Corporation Tax Law*; Art 141(1) and Art 141(3) of the *Corporation Tax Law Enforcement Order*

¶10-220 No credit for tax on highly taxed income of corporations

Japan does not allow a foreign tax credit for the portion of foreign corporation taxes which are imposed at a rate higher than 35% (CTL-EO Art 142-2(1)). The 35% rate is an approximation of the combined Japanese national and local tax burdens. However, the portion of foreign corporation taxes attributable to highly taxed income that is not allowed as a foreign tax credit may be deducted as an expense. Prior to a revision of regulations in 2011 in connection with reductions in the corporation tax burden in Japan, foreign corporation taxes that were imposed at a rate higher than 50% were not allowed for purposes of the foreign tax credit.

Law: Art 142-2(1) of the *Corporation Tax Law Enforcement Order*

¶10-221 Highly taxed interest income of corporations

Typically, a source country will tax interest income of a foreign corporation based on a percentage of gross interest. For Japanese companies with substantial interest revenues, a special ceiling rate is used to calculate the creditable foreign corporation tax amount for foreign withholding taxes levied on the gross amount of interest. The ceiling rate is the rate of tax on gross interest which approximates the tax on the interest when it

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is taxed in Japan on a net basis. The creditable foreign corporation tax amounts allowed for foreign withholding taxes on gross interest are determined based on the nature of the company's main business as set forth in the following table (CTL-EO Art 142-3(2)):

Table 1: Creditable foreign corporation tax amounts

Classification of main business	Income ratio (ratio of net income to gross income)	Maximum creditable foreign corporation tax amount
Finance and securities, life and casualty insurance companies	10% and less	Up to 10% of interest
	More than 10% and not more than 20%	Up to 15% of interest
	More than 20%	Full amount of tax
All other companies: Ratio of interest revenue to sum of interest revenue and gross profit is 20% or more	10% and less	Up to 10% of interest
	More than 10% and not more than 20%	Up to 15% of interest
	More than 20%	Full amount of tax
Ratio of interest revenue to the sum of interest revenue and gross profit is less than 20%		The special rule for withholding tax on interest does not apply

Law: Art 142-3(2) of the *Corporation Tax Law Enforcement Order*

¶10-230 Creditable foreign tax amount of corporations

The creditable foreign tax amount for corporations is equal to the amount of foreign taxes incurred during the year less the portion of the tax which exceeds 50% of the applicable foreign tax base (CTL-EO Art 142-3(1)). Each separate foreign tax is tested separately under this and the test is applied separately to national and local taxes (CTL Basic Circular 16-3-22).

Law: Art 142-3(1) of the *Corporation Tax Law Enforcement Order*

¶10-240 The foreign tax credit limitation

The Japanese foreign tax credit limitation is designed to prevent foreign taxes in excess of the corresponding Japanese tax amount from being used to reduce the Japanese tax on domestic income. The limitation is based on the taxpayer's overall foreign income and tax, separate country limits are not used. The amount of foreign taxes for the current tax year that a Japanese taxpayer can take as a credit is equal to the lesser of (ITL Art 95 (1); CTL Art 69(1)):

- the creditable foreign tax amount incurred during the year, or
- the amount of the foreign tax credit limitation.

The amount of the Foreign Tax Credit Limitation is calculated using the following formula (ITL-EO Art 222(1); CTL-EO Art 142(1)):

$$\text{Foreign tax credit limitation amount} = \text{Japanese Corporation Tax for the taxable year} \times \frac{\text{Foreign source income for the taxable year}}{\text{Income (worldwide) for the taxable year}}$$

Tax treaty income sourcing rules. If there is a difference in the sourcing of income between Japanese domestic income and foreign income due to the terms of an income tax treaty, the sourcing rule contained in the income tax treaty will take precedence (CTL Art 139). Regulations provide that where income is subject to tax outside Japan under the provisions of an income tax treaty, the income will be treated as foreign income for purposes of the foreign tax credit limitation (CTL-EO 142(4)(iii)).

The excess of creditable foreign tax amount over the amount of the foreign tax credit limitation may, subject to separate limitations, be credited against the taxpayer's Japanese prefectural and municipal Inhabitants Tax and the remainder may be carried forward for three years.

Exclusion of untaxed foreign source income of corporations

To prevent inflation of the foreign tax credit limitation amount with untaxed foreign source income, any untaxed foreign source income of a corporation is excluded from the calculation of foreign source income for the year, but remains included in income (worldwide) (CTL-EO Art 142(3)). Income of a designated tax haven subsidiary included in the income of a Japanese shareholder under the tax haven rules (see ¶9-600) that is located in a jurisdiction that does not impose tax, but whose income is subject to tax in a jurisdiction other than where its head office is located, is not treated as untaxed foreign source income for this purpose.

Ninety per cent ceiling on a corporation's foreign source income

When computing the credit limitation, foreign source income of a corporation is limited to 90% of the income (worldwide) for the year (CTL-EO Art 142(3)). This rule provides that Japanese tax will be paid on at least 10% of income.

Law: Art 69(1) and Art 139 of the *Corporation Tax Law*; Art 95(1) of the *Income Tax Law*; Art 142(1), Art 142(3) and Art 142(4)(iii) of the *Corporation Tax Law Enforcement Order*; Art 222(1) of the *Income Tax Law Enforcement Order*

¶10-250 Local tax limits on foreign tax credit

If the creditable foreign corporation tax amount exceeds the foreign tax credit limitation, to the extent of the local tax limitations, the excess creditable foreign corporation tax amount may be taken as a credit against prefectural and municipal Inhabitants Tax (*Local Tax Law* Art 53(11), Art 321-8(11)). However, the foreign tax credit is not allowed to reduce the per capita part of the Inhabitants or the Enterprise Tax.

The Local Tax limits on the foreign tax credit are determined as percentages of the applicable foreign tax limits under the Income Tax or Corporation Tax, depending on the taxpayer as indicated in the following table.

Table 2: Local tax limits on foreign tax credit

	Municipal Inhabitants Tax foreign tax credit limit	Prefectural Inhabitants Tax foreign tax credit limit
Income Tax	20% of the limit under the Income Tax (LTL Art 314-7; LTL-EO Art 48-9-2)	10% of the limit under the Income Tax (LTL Art 37-2; LTL-EO Art 7-19)
Corporation Tax	12.3% of the limit under the Corporation Tax (LTL Art 321-8 (29))	5% of the limit under the Corporation Tax (LTL Art 53(1) (59))

Law: Art 37-2, Art 53(1)(59), Art 53(11), Art 314-7, Art 321-8(1) and Art 321-8(29) of the *Local Tax Law*; Art 7-19 and Art 48-9-2 of the *Local Tax Law Enforcement Order*

¶10-260 Carryovers of foreign tax credit benefits

Taxpayers may carry forward for three years the national and local tax foreign tax credit limitation amounts that are not used in the current taxable year (ITL Art 95(2); CTL Art 69(2)). Taxpayers may also carry forward for three years excess creditable foreign tax amounts (ITL Art 95(3); CTL Art 69(3)).

Loss of carryovers

If a taxpayer elects to take a deduction for the foreign taxes instead of the credit, all credit limitation carryover amounts and creditable foreign corporation tax carryover amounts originating in that or any prior year are extinguished and may not be used in the current or any future year (ITL-EO Art 224(2) and Art 225(2); CTL-EO Art 144(2) and Art 145(2)). However, carryovers are not affected by the deduction of foreign taxes attributable to highly taxed income (see ¶10-220).

Law: Art 69(2) and Art 69(3) of the *Corporation Tax Law*; Art 95(2) and Art 95(3) of the *Income Tax Law*; Art 144(2) and Art 145(2) of the *Corporation Tax Law Enforcement Order*; Art 224(2) and Art 225(2) of the *Income Tax Law Enforcement Order*

¶10-270 The foreign dividend exemption system

The indirect foreign tax credit system applicable before 1 April 2009 allowed a foreign tax credit to the parent for the foreign tax deemed paid on the dividend received from a foreign subsidiary if the parent owned at least 25% of the subsidiary's stock (CTL Art 69(8)). Effective for tax years beginning on or after 1 April 2009, the indirect foreign tax credit has been replaced by a system of exempting 95% of foreign dividends from the income of the Japanese company shareholder (see ¶4-633).

Law: Art 69(8) of the *Corporation Tax Law*

¶10-275 Credit for taxes paid by second-tier subsidiaries

The creditable foreign tax amount deemed paid by a Japanese parent company may also include foreign taxes incurred by second-tier foreign subsidiaries when the second-tier subsidiary pays dividends to a first-tier subsidiary (CTL Art 69(11)). The indirect foreign tax credit rules are inapplicable to taxes paid by third and lower-tier subsidiaries.