Interim Report of the Study Group on International Taxation in the Digital Economy (Summary)

In order for Japan to continue its sustainable growth as an "investment nation" *, from the viewpoint of constructing a tax system that enables Japanese companies to fairly compete with foreign companies inside and outside of Japan, the Study Group will consider formulating international agreements at the OECD/G20 and other fora (global minimum tax, etc.) into domestic laws as well as remaining issues (Taxation, etc., on foreign companies, etc., in the domestic digital market) (Chair: Eiji TAJIKA, Professor Emeritus, Hitotsubashi University).

*The income balance of dividends from overseas subsidiaries to parent companies (approx. JPY 20.1 T) contributed to the current account surplus (approx. JPY 20 T)

Competitive Situation and Basic Concept of Japanese Companies

- In domestic and overseas markets, the Japanese companies face challenges in price competitiveness and product development capabilities compared with foreign companies. Foreign companies are monopolizing or oligopolizing the domestic digital market.
- There is a large tax burden gap with digital companies that do not have branches, etc., in market jurisdictions/that transfer intangible assets to jurisdictions with no or low-tax burden for tax avoidance.

- **Reforming the international taxation system will create an environment of fair competition between Japanese and foreign companies in domestic and foreign markets.** By doing so, **Japanese companies will be able to secure cash flow, which will be used as a source of investment, and strengthen their international competitiveness by promoting risk investment.**

Background and direction of international discussions

Allocation of taxing right to market jurisdictions (Pillar 1)

[Current situation] No taxation is allowed in a market jurisdiction because there are no PEs such as branches.

[Response] Allocating a portion of the profits of large, high-profit multinational enterprises to market jurisdictions. Adjusting for the removal of Digital Service Taxes(DST), etc.

Global Minimum Tax (Pillar 2)

[Current situation] Intangible assets that are the source of income are transferred to subsidiaries in no or low-tax jurisdictions and cannot be taxed in the home country. This will lead to competition to lower the corporate tax rate.

[Response] A minimum tax rate (at least 15%) is set, and the shortfall of foreign subsidiaries is additionally taxed in the home country.

Direction of future measures

- **We look forward to the early entry into force of the international agreement (Pillar 1).**
- The following were examined as remaining problems.
  - **Appropriation of consumption tax** on **cross-border transactions(Online games, etc.)by foreign companies**.
  - **Strengthen measures against tax avoidance by Japanese subsidiaries of foreign companies** as necessary.
  - **The need to consider measures to be taken in case Pillar 1 takes effect late** is also pointed out.

- **If major jurisdictions introduce global minimum tax, it will contribute to fair competition on a global basis.**
- Consideration could be given to the following in the final agreement and domestic legislation in the future.
  - **The timing of introduction is based on relationships with** major **competitors (Europe, China, South Korea, etc.).**
  - **Consideration for the tax burden of substantial** local **businesses (manufacturing, etc.).**
  - **Adjustment and simplification of the relationship with the existing CFC rules.** Facilitating global business activities such as overseas M&A, etc.
  - Tax system to **promote the formation and use of intangible assets in Japan.**