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Okamoto & Company International Accounting Office / Hanato Tax Accountant Office

OKAMOTO & COMPANY

## J-GAAP

Accounting for Asset Retirement Obligations (hereafter "AROs") has been required under International Financial Reporting Standards (IFRS), IFRS for small and medium-sized entities and U.S. GAAP and will now be required under Japan GAAP. There is no requirement to record AROs for small and medium-sized entities accounting and those reported under tax-basis accounting in Japan. The Accounting Standards Board of Japan (ASBJ) issued an "Accounting Standards for AROs (ASBJ Statement No. 18)" and " Guidance on Accounting Standards for AROs (ASBJ Guidance No. 21)", which shall apply to fiscal years beginning on or after April 1, 2010. Early adoption is permitted. An ARO is a statutory or similar obligation with regards to the costs of removal of fixed assets and is initially recorded when the assets are acquired, constructed, developed or used in normal business operations. Retirement of the asset is defined as the cessation of the use of the asset. This is based on estimates of the undiscounted future cash flow required for the removal of the relevant asset. Cases where the amount of the obligation cannot be reasonably estimated initially, when it becomes possible to reasonably estimate the amount of the obligation, it should be recognized as a liability.

## Japanese Taxes

As of the date of this newsletter, Parliament has not yet ratified the 2011Tax Reform Act. It appears the much publicized 5% decrease in corporate income tax rates will be excluded from this year's Act. The major points of the Act in debate, which will likely be of interest to our clients are as follows:

### Corporate Taxes

1. Depreciation

For assets purchased on or after April 1, 2011, the rate of acceleration on the declining balance method has decreased from 250% to 200%.

2. Carry-forward of taxable losses

From fiscal periods beginning on or after April 1, 2011, only 80% of the periods' taxable income can be offset with taxable losses carried forward from the previous periods. This 80% ceiling will not apply to companies with capital 100 million yen or less. At the same time, the carry-forward period of taxable losses increased to 9 years from 7 years.

### Consumption Taxes

1. Conditions to be exempt enterprises

Under the current rules, if taxable sales did not exceed 10 million yen two years prior (i.e. base period) to the current period, enterprises were exempt from filing consumption tax returns. However, under the new rules, an entity must also look at the first six months of the prior year. If sales for the first six months of the prior fiscal year exceeds 10 million yen, the enterprise must file a consumption tax return for the current period.

2. Credit for taxable purchases

For companies with taxable sales of 500 million yen or more, enterprises may no longer be able to claim back 100% of the prepaid consumption taxes. Under the current rules, if taxable sales comprised 95% or more of the total sales, the enterprise was able to claim all of the prepaid consumption taxes. However, for periods beginning on or after April 1, 2012, such enterprises will only be able to apply the same percentage of taxable sales against prepaid consumption taxes.

### Individual Income Taxes

1. Employment Income Deduction

A. Limitation of employment income deduction

A new ceiling has been introduced for employment income deductions. For individuals with gross income in excess of 15 million yen, the employment income deduction is capped at 2.45 million yen.

For example, income taxes for an individual with 17 million yen of gross salary would be computed under the following method:

(Unit : in thousands of yen)

| | Current (A) | Amended (B) | Diff (B) – (A) |
|---|---|---|---|
| Gross employment income | 17,000 | 17,000 | – |
| Employment deduction | (2,550) | (2,450) | (100) |
| Taxable income | 14,450 | 14,550 | 100 |
| Income tax (33%) | 3,232.5 | 3,265.5 | 33 |

B. Directors' remuneration

In addition to A above, employment income deduction for directors will decrease when the employment income exceeds 20 million yen as shown at the table below:

| Gross employment income (in Yen) | New deduction computation |
|---|---|
| 20 M – 25M | 2.45 M – (Gross salary—20 M) x 12% |
| 25 M – 35M | 1.85 M |
| 35M – 40M | 1.85 M – (Gross salary—35 M) x 12% |
| Over 40M | 1.25 M |

For example, employment deduction for a director with 40 million yen of gross salary would be:

(Unit : in thousands of yen)

| Previously | Amended | Decrease |
|---|---|---|
| 40,000 x 5% + 1,700 = 3,700 | 1,250 | 2,450 |

2. Severance Pay

A. Severance pay to directors

For severance paid to directors who served under five years, the calculation of taxable retirement income has changed for national individual tax purposes. Before the amendment, taxable retirement income was multiplied by 50% of the paid benefits after the retirement income deduction. Under the new rule, the 50% reduced rate can no longer be applied. This amendment is effective from January, 2012.

B. Inhabitant taxes for severance pay

The tax rate of local individual taxes for retirement income will return to 10% from 9%. This change applies to all employees and directors who receive benefits.

3. Dependency Deduction

| Age | Previously | 2010 Amendment | 2011 Amendment |
|---|---|---|---|
| 70 and over | 480,000 | 480,000 | 480,000 |
| 65 – 70 | 380,000 | 380,000 | 380,000 |
| 23 – 65 | 380,000 | 380,000 | 380,000* |
| 19 – 23 | 630,000 | 630,000 | 630,000 |
| 16 – 19 | 630,000 | 380,000 | 380,000 |
| Younger than 16 | 380,000 | – | – |

* - If a taxpayer's income is above four million yen, there is no dependency deduction.

## Payroll

Effective March 2011, the health insurance rates have changed as follows:

Health Insurance (based on the Health Insurance Association-Tokyo)
Employer contribution - from 4.66% to 4.74%.
Employee contribution - from 4.66% to 4.74%.

Care Insurance
Employer contribution - from 0.75% to 0.755%.
Employee contribution - from 0.75% to 0.755%.

Some of the health insurance unions also modified its rates. For example, ITS (Software) Kenpo:

Employer contribution - from 3.5% to 4.25%.
Employee contribution - from 3.5% to 4.25%.

### Care Insurance

No change from 1% (0.5% each for employer and employee)

### Compensation during Rolling Blackouts

If employers paid employees who are ordered not to go to work "absence from work" during rolling blackouts based on labor contracts or employment rules, and if they later changed the status to unpaid leave, it will be classified as a disadvantageous change in working conditions and will not be in complacence with Japanese Labor Lows.
However, if such absence from work was already defined as unpaid leave, employers are not required to make payment under Japanese Labor Laws.

If there is absence from work due to reasons other than rolling blackouts, employers should take whatever steps possible to avoid closing their business. If employers conclude that working around rolling blackouts during the day would be impractical (and the employer can support such decision), employers will not have an obligation to pay the employees for time surrounding blackouts. (Please contact the respective Labor Standards Supervision for details).

Please access the following URL for further information:

http://www.mhlw.go.jp/stf/houdou/2r98520000016u30-img/2r98520000017eok.pdf

(Q&A (ver2) regarding the Labor Standards Act and related Acts on 2011 Japan Tohoku Earthquake)

## Preparing for the Worst

1. Data Backup

In the event of a natural disaster or rolling blackouts, it is critical to backup of your data. For many foreign subsidiaries, there are an increasing number of parent companies who perform backups of their subsidiary's data. If this is not being performed at your company, preparations should be made to backup the data periodically. The importance of the backup data should be considered in developing the frequency, location of the data and types of hardware.

For sudden power outages, UPS (Uninterruptible Power Supply) systems can keep crucial systems running for a short period of time. If blackouts are expected for over 30 minutes (e.g. rolling blackouts), portable generators should be considered. If you have an analog telephone line, analog telephones could be useful since it does not require electricity.

2. Disaster Prevention Links

The Japan Tohoku earthquake was followed by many aftershocks. We never know when the next large earthquake will hit. We listed some disaster prevention links, which might be useful.

For individuals

https://www.kitakumap.com/information/preparation.html
(preparations on a routine basis)

For corporations

http://www.tokyo-cci.or.jp/chiiki/bcp/bcp5.pdf
(Tokyo version "Small, Medium Sized Company BCP step-up guide" evaluation checklist)

Local disaster prevention measures
http://www.bousai.metro.tokyo.jp/ (Disaster prevention information HP of Tokyo Metropolitan Government Bureau of General Affairs)

It is also important to confirm the above matters with the owner/administrator of your building before implementation.

## OMC (Office Manager Club)

Hiroko Hanato, partner, launched an information site for office managers at foreign companies who are involved in accounting, general administration, and HR activities. The website will feature a broad range of useful information about audits, accounting, social insurance and tax for members. Registration is free. For those interested, please access http://www.omckyoto.com/.

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