Tax Insights & Commentary

What do Japanese Companies Think About the GloBE Rules?

By Takato Masuda

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Takato Masuda of Nishimura & Asahi provides an insight into a recent report on the views of the Japanese business sector on the Organisation for Economic Co-operation and Development global minimum tax rules (Pillar Two) and the controlled foreign corporation regime.

On Sept. 1, the Ministry of Economy, Trade, and Industry (METI) of Japan published the report (in Japanese only) issued by the Study Group on the Global Minimum Tax and CFC Regime. The report provides valuable insights into how the Japanese business sector views the global minimum tax (Pillar Two) and the controlled foreign corporation (CFC) regime.

The Study Group and its Background

The study group comprises 13 members—four academics, two tax professionals, and seven companies, including Toyota and SONY. In addition, major economic organizations such as Keidanren (Japan Business Federation), and relevant authorities such as the Ministry of Finance and the Japanese tax agency, also participated as observers.

METI is not directly in charge of tax reform. Thus, the ministry might intend to formulate the message from the business sector, with the involvement of academics and tax professionals, through this study group, and deliver it to those in charge of relevant potential tax reforms.

According to the ministry's press release, the study group mainly addressed two issues: (1) the smooth introduction of the Global Anti-Base Erosion Model Rules (GloBE rules) in Japan; and (2) the simplification of the CFC regime.

Why does the simplification of the CFC regime matter here? According to the report, the logic behind this is as follows:

1. The global minimum tax will ensure a level playing field for Japanese and foreign companies; however, it inevitably requires additional administrative work for Japanese companies.
2. Compliance costs should be within a reasonably permissible range; therefore, an optimized implementation of the GloBE rules and simplifying the existing CFC regime should be undertaken.

In practical terms, the second agenda item, simplifying the CFC regime, should have a higher priority than the first, introducing the GloBE rules smoothly. This is because the Japanese version of the GloBE rules must conform to internationally agreed model rules, which limits the scope for Japan to design its own rules.

Overview of the Report

The main body of the report roughly consists of two parts corresponding to the above points. The first part enumerates issues to be addressed in adopting the GloBE rules into domestic law. The second part contains some ideas for narrowing the scope of the Japanese CFC regime.

The report is summarized below, (based on the executive summary slide of the report).

1. Introduction of the GloBE Rules

1. The simplification options proposed in the OECD Blueprint should be adopted. A qualified domestic minimum top-up tax must be designed with minimal compliance costs for Japanese companies if Japan introduces it.
2. An even more straightforward set of rules is needed for domestic legislation; several issues remain unresolved in the model rules.
3. The effective date of the domestic rules should be determined by considering those of economically competing countries as well as the time required for preparation.
4. The due date for filing and paying the global minimum tax should be later than the GloBE Information Return deadline (i.e. 15 (or 18) months after the last day of the Reporting Fiscal Year).

2. Simplification of the CFC Regime

1. A company has to review many CFCs but usually finds only a few are in scope. It may be possible to add objective thresholds which reduce the number of companies to be reviewed.
2. The economic activity test is sometimes unreliable and often burdensome to undertake. Even CFCs with substantial economic activity may be unable to pass this test. It may be worthwhile to revise the test in some way.
3. Collecting information separately for GloBE Rules purposes and for CFC regime purposes would result in high compliance costs. The information gathered for the former could possibly be used for the latter.
4. The current CFC tax regime can impose severe time constraints on companies, especially when the subsidiary's fiscal year end is close to the parent company's tax filing deadline. The time frame under the CFC regime should be expanded.

What do Japanese Companies Seem to be Thinking?

Introduction of the GloBE Rules

According to the report, the basic policy should be to "support the international business activities of Japanese companies by ensuring a level playing field between Japanese and foreign companies," while "minimizing the burden of those Japanese companies." As such, the GloBE rules are generally viewed as beneficial to Japanese enterprises.

The report also strongly calls for simplification and clarification of the rules as much as possible; otherwise, compliance costs will exceed acceptable levels, even taking into consideration the above advantages.

Simplification of the CFC Regime

The report spends more time on the discussion of simplifying the CFC regime rather than introducing the GloBE rules; this probably reflects Japanese companies' strong interest in revising the CFC regime. Nevertheless, there is currently no clear consensus on what kind of simplification (narrowing the scope) would meet the needs of companies without causing under-inclusion. The report listed the participants' opinions (without specifying the speaker) and pointed out some issues to be addressed in future discussions.

Next Steps

At the end of August, METI submitted the relevant revision requests to the Ministry of Finance as part of the annual routine steps for tax reform. After negotiations between the two ministries and debate in the ruling party's research commission on the tax system, the revision proposals will be finalized—or withdrawn or postponed—by the end of this year. The revision debate has just begun; it will likely involve additional studies to make the proposal more concrete and feasible.

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