Narrative Report on Japan

Japan, the world’s fourth largest economy on a purchasing power parity basis, is ranked at 10th position on the 2013 Financial Secrecy Index. This ranking is based on a combination of its secrecy score and a scale weighting based on its share of the global market for offshore financial services.

Japan has been assessed with 61 secrecy points out of a potential 100, which places it in the mid-range of the secrecy scale (see chart 1).

Japan accounts for over 1 per cent of the global market for offshore financial services, making it a small player compared with other secrecy jurisdictions (see chart 2).

Part 1: Telling the story
30 September 2013

Japan is not widely regarded as a secrecy jurisdiction, but it is appropriate to include it in our index.

Japan’s “Big Bang” in terms of offshore finance happened with the setting up of the so-called Japan Offshore Market in 1986. Essentially, this was an effort to attract foreign financial business by exempting it from tax and a range of financial regulations. It was modeled on a Singaporean facility (the Asian Currency Market) that had been set up in 1968, and on a similar U.S. facility set up by the United States in 1984. More generally, it was also a reaction to the rapid growth of the offshore Euromarkets, pioneered by the City of London since the 1950s (Treasure Islands pp 80-102). This was followed by special tax exemptions for Japanese government bonds in 1999, and for municipal bonds in 2007. The scope of the tax exemption was widened in 2010 to include corporate bonds.

Japan’s fairly weak provisions on transparency and information exchange, combined with its tax-free treatment of various forms of foreign investment and exemption from financial regulations, have made it a significant destination for illicit financial flows. The country’s relatively poor record of co-operation with foreign governments on money-laundering adds to our concerns.
Japan does, however, place some restrictions on non-residents wishing to open bank accounts, and customer due diligence makes it harder than in many jurisdictions for illicit funds to enter and be banked in Japan under anonymous or third party names.

Japan has also taken measures to protect itself against offshore tax haven activity. In 1978 it adopted a Tax Haven Counter Measure Law (THCML, amended a few times since then.) A part of the law since inception has been an “economic logic test” to the use of foreign subsidiaries by companies based in Japan. This has the objective of minimizing the potential of transfer pricing abuse, as also the use of tax havens or low tax jurisdictions. In essence, if the standards of the Business Purpose test are not met, the income is taxed currently at the parent company rates in Japan. These standards require that (i) the overseas subsidiary has sufficient staff, assets, and premises to execute business in the jurisdiction concerned, (ii) that it has local management and control of the business, and (iii) more than 50% of its income is derived from sources that are not part of its related group of companies including the parent. As a result of these requirements the use of tax havens and low-tax jurisdictions is limited in scope for Japanese multinational companies. (For more details, see http://japantax.org/?p=590, and access the Japan tax haven rules.)

Next steps for Japan

Japan’s 61 per cent secrecy score shows that it must still make major progress in offering satisfactory financial transparency. If it wishes to play a full part in the modern financial community and to impede and deter illicit financial flows, including flows originating from tax evasion, aggressive tax avoidance practices, corrupt practices and criminal activities, it should take action on the points noted where it falls short of acceptable international standards. See part 2 below for details of Japan’s shortcomings on transparency. See this link http://www.financialsecrecyindex.com/kfsi for an overview of how each of these shortcomings can be fixed.

Part 2: Secrecy Scores

The secrecy score of 61 per cent for Japan has been computed by assessing the jurisdiction’s performance on the 15 Key Financial Secrecy Indicators, listed below.
The numbers on the horizontal axis of the bar chart on the left refer to the Key Financial Secrecy Indicators (KFSI). The presence of a blue bar indicates a positive answer, as does blue text in the KFSI list below. The presence of a red bar indicates a negative answer as does red text in the KFSI list. Where the jurisdiction’s performance partly, but not fully complies with a Key Financial Secrecy Indicator, the text is coloured violet in the list below (combination of red and blue).

This paper draws on key data collected on Japan. Our data sources include regulatory reports, legislation, regulation and news available at 31.12.2012. The full data set is available here. Our assessment is based on the 15 Key Financial Secrecy Indicators (KFSIs, below), reflecting the legal and financial arrangements of Japan. Details of these indicators are noted in the following table and all background data can be found on the Financial Secrecy Index website.

The Key Financial Secrecy Indicators and the performance of Japan are:

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<th>TRANSPARENCY OF BENEFICIAL OWNERSHIP – Japan</th>
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<tr>
<td>1. Banking Secrecy: Does the jurisdiction have banking secrecy?</td>
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<tr>
<td><strong>Japan does not adequately curtail banking secrecy</strong></td>
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<tr>
<td>2. Trust and Foundations Register: Is there a public register of trusts/foundations, or are trusts/foundations prevented?</td>
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<tr>
<td><strong>Japan partly discloses or prevents trusts and private foundations</strong></td>
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3. Recorded Company Ownership: Does the relevant authority obtain and keep updated details of the beneficial ownership of companies?

Japan does not maintain company ownership details in official records

### KEY ASPECTS OF CORPORATE TRANSPARENCY REGULATION – Japan

4. Public Company Ownership: Does the relevant authority make details of ownership of companies available on public record online for less than US$10/€10?

Japan does not require that company ownership details are publicly available online

5. Public Company Accounts: Does the relevant authority require that company accounts are made available for inspection by anyone for a fee of less than US$10/€10?

Japan does not require that company accounts be available on public record

6. Country-by-Country Reporting: Are all companies required to comply with country-by-country financial reporting?

Japan does not require country-by-country financial reporting by all companies

### EFFICIENCY OF TAX AND FINANCIAL REGULATION – Japan

7. Fit for Information Exchange: Are resident paying agents required to report to the domestic tax administration information on payments to non-residents?

Japan requires resident paying agents to tell the domestic tax authorities about payments to non-residents

8. Efficiency of Tax Administration: Does the tax administration use taxpayer identifiers for analysing information efficiently, and is there a large taxpayer unit?

Japan partly uses appropriate tools for efficiently analysing tax related information

9. Avoids Promoting Tax Evasion: Does the jurisdiction grant unilateral tax credits for foreign tax payments?

Japan partly avoids promoting tax evasion via a tax credit system

10. Harmful Legal Vehicles: Does the jurisdiction allow cell companies and trusts with flee clauses?

Japan partly allows harmful legal vehicles
**INTERNATIONAL STANDARDS AND COOPERATION – Japan**

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| **11.** | Anti-Money Laundering: Does the jurisdiction comply with the FATF recommendations?  
Japan does not comply with international anti-money laundering standards |
| **12.** | Automatic Information Exchange: Does the jurisdiction participate fully in Automatic Information Exchange such as the European Savings Tax Directive?  
Japan does not participate fully in Automatic Information Exchange |
| **13.** | Bilateral Treaties: Does the jurisdiction have at least 46 bilateral treaties providing for information exchange upon request, or is it part of the European Council/OECD convention?  
As of 31 May, 2012, Japan had less than 46 tax information sharing agreements complying with basic OECD requirements |
| **14.** | International Transparency Commitments: Has the jurisdiction ratified the five most relevant international treaties relating to financial transparency?  
Japan has partly ratified relevant international treaties relating to financial transparency |
| **15.** | International Judicial Cooperation: Does the jurisdiction cooperate with other states on money laundering and other criminal issues?  
Japan does not cooperate with other states on money laundering and other criminal issues |

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1. With the exception of KFSI 13 for which the cut-off date is 31.05.2013. For more details, look at the endnote number 2 in the corresponding KFSI-paper here:  