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**Policy Guidance on the Establishment of a Desirable Tax System
(Draft)**

The Tax Commission

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Introduction

At the beginning of this 21st century, Japan is reaching a critical stage to make a comprehensive tax reform since the basic policy and framework of the present tax system greatly depend on the Shoup Taxation System introduced in 1950. Since then a half-century has passed, and the Japanese economic system, formed after World War II, has been undergoing great changes. In anticipation of a coming aging society, a number of comprehensive tax reforms have been introduced, including the introduction of consumption tax and the relaxation of progressive taxation of individual incomes. However, the present tax system is unable to deal appropriately with rapid changes of the Japanese socioeconomic structure, for example the falling birthrate, aging population, and globalization of economic activities. Thus, considering the transforming Japanese society, it is essential to institute a long-range tax reform that is applicable to the Japanese society over a couple of decades to come.

Based on a request for deliberation made in September 2000 by then Prime Minister Mori, the Tax Commission set up a Sub-Committee on Basic Issues in July 2001 to discuss a medium- and long-term tax system. Since the request from Prime Minister Koizumi in January 2002, the commission started intensive deliberation on fundamental reform of the tax system of this country from mid- to longer-term viewpoints. The Tax Commission has been discussing the reform and, based also on the discussions at the tax town meetings held at six places in Japan, decided to publish the policy guidance on the establishment of a desirable tax system. Specifically, Prime Minister Koizumi asked the Tax Commission to examine the existing tax system "without prejudgment" and "without

sanctuaries” from the medium- and long-term viewpoints for structural reform. The prime minister also added that if the commission recommends a tax reform for a short-term economic vitalization, the reform must be consistent with the basic medium- and long-term policies for tax reform. His requests were completely in line with the directions for which the Tax Commission has been pursuing so far.

The Tax Commission worked on the examination of the existing tax system from medium- and long-term viewpoints rather than a short-term viewpoint so that a reformed tax system could be instituted to function well in the first half of the 21st century in Japan. This draft depicts basic policies of a desirable tax system. The ongoing examinations will decide more concrete contents of taxes to be re-examined and the timing of reforms at a later stage.

The contents of the reform will be broad and comprehensive because what is being proposed is a comprehensive reform of tax system that was instituted some 50 years ago. As a result of adjusting deficiencies in the existing structure, tax may increase in a number of areas. Needless to say, however, the Tax Commission has no intention to recommend that this tax reform be legislated immediately for FY2002 or FY2003. A tax reform must be introduced into society gradually and carefully. It is essential that the government carry out a thorough cut in expenditures and administrative reforms in enforcing a tax reform in order to gain trust and support from Japanese people. Such austere measures will include cuts in expenditures for social security, public works, and budgets for local governments. Visible and thorough cuts in expenditures seem inevitable in order to gain support from taxpayers. In addition, discussions must be continued to deepen discussion on a sustainable and efficient social security system.

This report intends to outline, from the mid-to-longer term viewpoints, policies toward establishing a desirable tax system for Japan that has a large fiscal deficit amid the falling birthrate and aging society. . The Tax Commission welcomes broad and constructive discussions on reforming tax system toward a desirable tax system.

Part I. Basic Policy

1. Establishing a Desirable Tax System for Vitalizing the Socioeconomy

At the beginning of this 21st century, the Japanese socioeconomy is experiencing radical changes including the falling birthrate, aging population, diverse lifestyles, globalization, computerization, growing stock economy, and people's increasing awareness of environmental issues such as global warming. In particular, the falling birthrate and aging population have continued at a rate faster than expected. According to a newest estimate of population, the birthrate will still continue to fall. As a result, the Japanese population will reach the peak in 2006 and then begin to decrease. The number of working people is also expected to continue to decrease in the future. Amid rapidly developing computerization and globalization, companies have to compete worldwide.

An increasing number of Japanese people are anxious about the future of the socioeconomy. Unless Japan can successfully cope with its structural changes, the nation would not be able to revitalize its economy and remain sluggish for a long time to come amid the falling birthrate, aging population, and decrease in the number of working people. In order to keep the socioeconomy vital and sustainable, Japan is urged to accomplish a broad range of structural reforms, including legal system reforms. Tax

reform is also a part of such structural and legal system reforms. The Japanese government needs to show its people a clear picture of medium- and long-term structural reforms and go down the road. These efforts alone will win people's support to the government and restore people's confidence and will to revitalize socioeconomy.

2. Viewpoints for Establishing a Desirable Tax System

In discussing an appropriate tax system for a vital socioeconomy, principles of "fairness, neutrality, and simplicity of taxation" (see the appendix) shall continue to remain the key. In particular, given the situation of Japan discussed above, the following four standpoints should be taken into account.

1) Tax System That Allows Free Economic Activities - Efficient

distribution of resources and well-targeted policies -

Through high-economic growth (1960s and 70s), Japan formed a uniformed socioeconomy where the government policy-led measures played an important role. Taxation was no exception. Special taxation measures to advance particular policies have been taken. However, market economy has penetrated worldwide in the 21st century and people's sense of value has become diverse in the socioeconomy. Efficient distribution of resources through the market led by the private sector must be realized more thoroughly than before. An appropriate tax system must be fair and neutral in economic activities and support the freedom of individuals and corporations as well. Based on these standpoints, the Japanese government should rationalize and streamline existing special taxation measures should be concentrated only in truly effective areas.

2) Proper and Simplified Taxation – Gaining Public Support and Promote Participation of General Public in the Society-

If our tax system fails to cope with structural changes, such as the falling birthrate and aging population, and is unable to correct the existing tax measures that cause unfair burdens of taxes and feelings of unfairness, Japan could gradually lose its social vitality because taxpayers feel discouraged to pay tax according to the unfair tax system. Thus, the government needs to correct such unfair tax measures from the standpoint that everyone should bear common social costs fairly.

In addition, appropriate taxation should include not only aspects in tax legislation but also aspects in tax enforcement in order to gain taxpayers' trust in tax system. In other words, a simplified tax system for taxpayers needs to be instituted. A simplified tax system can improve predictability of tax consequence of economic activities and contribute to the vitalization of the socioeconomy through lower tax compliance costs.

3) Achieving A Stable Revenue Structure – Establishing a sustainable financial base and eliminating people's anxiety for the future-

It is important to build a stable structure of the government's revenues in order to make the socioeconomy vital and sustainable. The Japanese government and local governments together have huge long-term outstanding debts (which are expected to reach ¥693 trillion for FY 2002, accounting for 140% of GDP). What is worse, such debts are still expected to continue to accumulate in the coming years. Naturally, the coming generations will be burdened with the debts. Even if the government succeeds in reforming the present social security system, the falling birthrate and aging population will bring about increase in payments for pensions and medical care benefits. The government's budget for FY 2002

expenditures totals ¥81 trillion while the tax revenue for FY 2002 stands only ¥47 trillion. The ratio of tax and social security to National Income (national burden ratio) is lowest among major countries. In other words, taxes collected by the Japanese government are insufficient to fulfill the role that taxes must bear all of the common social costs (revenue raising function of tax system).

A growing number of Japanese are worrying about the continued imbalance of the government budget and have become anxious about the future. In order to dispel the uneasiness and restore vitality in the socioeconomy, it is important to build a stable revenue structure, which can afford necessary public services.

The Japanese government is urged to attain the primary balance in pursuit of sustainable finance at earliest in the beginning of the 21st century. To this end, rigorous cuts in government expenditures are essential. Raising taxes is also inevitable.

Since the present Japanese economy is unfavorable, raising taxes is unlikely to come up as the urgent agenda. However, the ongoing examinations for tax reform must, at least, be compatible with these directions. Even if the government is going to introduce tax reduction in a truly effective manner to vitalize the nation's economy, on the other hand, it should be coupled with a concrete tax increase program so that the government's financial condition won't be deteriorated any more.

4) Local Taxation to Meet Needs of Enhanced Local Autonomy

Local taxes must be borne by people in the community according to their capacity to pay tax and benefits received in order to bear costs of administrative services provided by local governments. Thus it is desirable to share the burden thinly and broadly by inhabitants for benefits they

enjoy. And revenues from local taxes should be stable. In addition, it is also important to institute a tax system where tax autonomy of local governments can be exercised easily.

The present local taxation has a wide gap with reality throughout Japan. Expenditures and tax revenues of local governments are imbalanced. In addition, the ratio of individuals and corporations that pay no taxes accounts for a considerable percentage, which hurts benefit principle in local taxation. In particular, tax revenues of prefectural and municipality governments are quite unstable.

Under the circumstances, Japan is urged to promote decentralization as an important pillar of structural reform, to institute a self-supporting relation between the central government and local governments, and to realize vital and characteristic local societies. In order to help the formation of self-supportive local governments, effectiveness in local public finance and administration should be improved through mergers of local governments, and discontinuance and reduction of the central government's involvement in expenditures of local governments. Further, on condition of this, revenue base of local governments should be more self-supportive so that at their discretion and responsibility, and based on understanding by local taxpayers of the relationship between benefits and burdens of local administration through disclosure of local administrative information, local governments can provide people in the community with administrative services that meet local needs.

To this end, it is increasingly important for local governments to secure and consolidate local taxes from the standpoint of building a tax system that accompanies impartial and stable tax revenue sources of local governments.

3. Basic Design for a Desirable Tax System

From the standpoints of sharing the tax burden “thinly and broadly”, the Japanese government has introduced consumption tax, relief of progressive taxation at individual incomes, and reduction of corporation tax since the comprehensive tax reform measures were legislated in 1987 and 1988. When considering an appropriate tax system from the standpoints mentioned above, the main points of tax reform for the future should include the following:

The present individual income tax is at a quite low level as the result of past tax reduction measures. Thus, the individual income tax must restore its function as main tax. At the same time, exemptions and deductions must be revised in order to meet changes of the socioeconomy.

Corporation tax shall be based on a neutral tax system that ensures free activities of corporations amid ongoing globalization of economy. At the same time, the government should target and prioritize special taxation measures only at truly effective measures for the vitalization of the socioeconomy, while rationalizing and streamlining existing special taxation measures.

Consumption tax needs to play a greater role in the future when considering fairness between generations and vitality in the socioeconomy. Specifically, its scheme should be rationalized to gain the trust in the tax from people and its tax rate should be reviewed.

Inheritance tax and gift tax should be reviewed by lowering the top rate while broadening the taxation base in considering the function of redistributing wealth and ongoing falling birthrate, aging population, and expansion of stock economy. In addition, inheritance tax and gift tax should be consolidated in order to promote smooth passage of gifts from

living parents to their children.

Concerning the reform of local taxes, as a part of measures to improve the role of local taxes, and by taking into account of the review of roles and responsibilities of national and local governments, fundamental review of allocation of tax revenue sources - including transfer of taxation base from national government to local governments- should be conducted. The review should be conducted together with rationalization and streamlining of national subsidy and national contribution as well as review of effect of guaranteeing finance of local governments in local allocation tax (central government tax revenues allocated to local governments). Further, in conducting such review, impact of the changes on financial conditions of national government and individual local governments need to be considered when the revision is enforced. In addition, levels of tax burdens of national and local governments need to be reexamined.

In order to ensure benefit principle to local taxes, a number of measures could be considered, including revisions of exemptions and per-capita tax rates of individual inhabitant tax, introduction of taxation of enterprise tax by size of business of corporations, stabilizing and securing property tax, tax autonomy of local governments, etc.

By implementing the above-mentioned measures steadily, while ensuring an appropriate balance among income, consumption and property tax basis, establishing a desirable tax system of the 21st Century under which costs of the society is shared fairly and broadly, and through which, achieving sustainable vitalization of the socioeconomy.

Part II Reforms of Various Items of Tax

1. Taxation of Individual Income

1) Present Situation and Challenges of Individual Income Tax -

Restoring role as main tax -

Japan's individual income taxation (national tax: income tax, local tax: individual inhabitant tax) underwent several times of tax reductions. As a result, Japan's tax burden levels (the ratio of tax revenue to the national income, ratio of individual tax burden, etc.) are so low (limited scope of taxpayers paying tax at low rate), compared to other major countries. Individual income taxation is on the verge of losing the revenue raising function and the income redistribution function that individual income taxation is expected to play as main tax. In the review of the current individual income tax system, the above-mentioned problems of “hollowing out (shrinking tax base and revenue)” must be corrected in order to restore the original functions as main tax. At the same time, distorted distribution of tax burden, if any, amid the structural changes of the socioeconomy, ie. falling birthrate, aging population, must be corrected. In addition, "feelings of bearing unfair tax burden" that exist persistently among people must be solved correctly.

In the process of instituting a desirable individual income tax system, discussing increase in tax burden is unavoidable. In this case, a step-by-step introduction is essential for taxpayers to bear slow increase in tax burden.

2) Directions of the Reform in the Future

(1) Basic Policy - Sharing burden fairly and broadly -

a. Exemptions and deductions

Examples that indicate “hollowing out (shrinking tax base and

revenue) of Japan's individual income taxation” are found in the ratio of non-taxpayers to the total number of workers and relatively high lowest tax threshold (lowest taxable limit). Tax threshold is an accumulation of certain basic exemptions. The limit is the index to distinguish taxpayers from non-taxpayers and will affect the taxable income amount of all taxpayers. Beside the tax rate, taxable income is the most essential element affecting tax burden, revising exemptions is extremely important under the philosophy that "sharing expenses of the society fairly and broadly." The following three points will be important standpoints in revising exemptions.

- A. A variety of exemptions for income tax and individual inhabitant tax have been introduced in response to changes of living conditions including marriage, nursery, and old age. It is true that considering the circumstance of individual taxpayers is an important character of income tax and individual inhabitant tax. However, since various kinds of living "infrastructure" including social security have been implemented to a quite satisfactory level, it is appropriate to simplify and consolidate income tax and individual inhabitant tax.
- B. Instituting a neutral tax system is also quite important in order to avoid distorted sharing of tax burden among taxpayers and interference of free choices made by individuals in the socioeconomy amid ongoing structural changes, including the expanding gender-equal society, changes in employment practice, falling birthrate and aging population.
- C. Along with increase in aging population, reduction of the taxation base will be accelerated due to deduction for public pension, etc. To correct the "hollowing out" in the taxation base, it will be necessary

to revise exemptions in order to consolidate the taxation base.

b. Tax Rate Structure

Due to its reductions and simplification of bracket structure, Japan's minimum and maximum tax rates are lower compared with those of major advanced nations. In addition, the scope of income amounts where minimum tax rate is applied (bracket) has been expanded. For example, approximately 80% of Japanese taxpayers (employment income earners in the private sector) pay their income tax at minimum tax rate (10%), which is exceptional among the major advanced nations. In other words, the present income tax system in Japan allows most taxpayers to pay income tax at a quite low tax rate. This has been brought about by repeated alleviations of progressive taxation (flattening of tax bracket structure).

Progressive taxation is rather flat with individual inhabitant tax than income tax because the former asks burden according to the benefits that the taxpayer enjoy. Approximately 60% of taxpayers in Japan pay individual inhabitant tax at a minimum tax rate of 5%.

The progressive taxation was relaxed in the comprehensive tax reforms legislated in 1987 and 1988 where the taxation base was expanded, by including capital gains of securities, etc. into the tax base, but the tax rates were generally lowered by considering giving incentives for work and business, and stimulating the economy.

Further reduction of tax rates is inappropriate when the revenue raising function and income redistribution function of income taxation are taken into consideration. Rather, it will be an important option to cut back the bracket of the present minimum tax rate (see the appendix).

c. Permanent Tax Reduction

So-called "permanent tax reduction" of income tax and individual inhabitant tax has been implemented since 1999. The size of the reduction amounts about ¥4.1 trillion. Permanent tax reduction, especially the "fixed rate tax reduction" (about ¥3.5 trillion), was given by paying utmost consideration to economic situation, and thus, it should be repealed while paying attention to economic conditions.

(2) Reviewing Exemptions and Deductions

a. Exemptions for the Family Members

A. Streamlining and integrating of Personal Exemptions

(a) A variety of personal exemptions have been instituted in income tax and individual inhabitant tax by considering the family structure and other living conditions of individuals taxpayers. They are considered as reducing the ability to pay tax. These exemptions, however, should be revised from the standpoint mentioned in "2(1)a exemption" earlier and considering the following points:

a. A variety of "infrastructures" including social security and education have been well arranged compared with those when exemption measures were introduced for the first time. Meanwhile, because living conditions of individuals are different, introducing exemptions to meet individual conditions is naturally limited. In addition, Japanese people are generally satisfied with plentiful living facilities around them, and their senses of value on conditions for exemptions are becoming diverse.

b. Past repeated premiums and additional exemption measures

have resulted in a greater exemption for members of the family rather than the exemption for the taxpayer oneself. The exemption system has also become too complicated.

- (b) By implementing the following concrete measures for an appropriate tax system, exemptions should be simplified and consolidated into basic exemption, exemption for spouse, and exemption for dependent.
 - a. Specific dependant exemption, exemption for aged dependent, and other additional exemptions, and special exemptions such as exemption for working student, for widow(er), and other special exemptions should be simplified including discontinuance as much as possible. However, exemption for the disabled, which needs real consideration, should be continued.
 - b. A tax mechanism on special exemption for spouse has been introduced so that the exemption for the head of the household is reduced according to increase in the income of the spouse. This mechanism eliminates the unintentional decrease of the net income after-tax pay of the household, which is said the major cause of disincentive to work by part-time workers. However, the mechanism is based on exemption for spouse and special exemption for spouse, both of which are applied to the head of the household. Thus, the mechanism creates imbalance in exemptions for the head of the household and other dependent members of the family. In addition, this mechanism is pointed out as not neutral to social activities of men and women from the standpoint for the formation of gender-equal society. Based on the above-mentioned opinions and standpoints, it is

advisable to discontinue special exemption for spouse. In this case, the above-mentioned unintentional decrease of net income after-tax pay needs to be addressed.

B. Further Revision of the Basic Structure on Personal Exemptions

Further revision of the basic structure on personal exemptions, consisting of the three exemptions (basic exemption, exemption for spouse, and exemption for dependent), should be discussed and examined based on the following three typical different opinions for nationwide discussions.

In this case, Opinion 2 or Opinion 3 supposes that exemption for spouse and exemption for dependent are discontinued while basic exemption is upgraded and expanded.

[Opinion 1: Personal exemption should consist of the following: basic exemption, exemption for spouse, and exemption for dependent.]

Opinion 1 pays consideration to the purpose of the current personal exemptions, namely consideration to diminishing tax-bearing capacity due to support to dependents. The variation of this is to consolidating the personnel exemptions into family exemption (tentative title) and basic exemption in exchange of indiscriminating spouse from other dependent family members. Further, from the standpoint for forming gender-equal society, some members of the Tax Commission are of the opinion that exemption for spouse itself be abolished.

[Opinion 2: Exemption for spouse should be abolished and exemption for dependent should be limited to children and aged family members only.]

Opinion 2 is based on the idea that exemption, in principle, should

consist of only basic exemption of taxpayers themselves. Since the adult is supposed to have a capacity to work and have income, no exemption for dependent for the adult should be applied. Meanwhile, children and aged family members are regarded as having scarce opportunities for work, they should be included in exemption for dependent. This opinion accompanies the problem that no consideration is paid to diminishing ability to pay tax of a taxpayer and that a taxpayer is supposed to pay a sharply increased tax when his or her dependent family member reaches maturity age and no exemption for dependent is applied to the taxpayer.

[Opinion 3: Exemption for spouse and exemption for dependent should be abolished while tax credit for supporting children should be instituted.]

Opinion 3 adopts the idea that exemption should consist of basic exemption of the taxpayer alone while paying attention to supporting children in the form of tax credit. Unlike income exemption, this measure will allow the equal amount of tax benefit regardless of the amount of income of a taxpayer (however, the measure do not benefit non-taxpayers). As this opinion pays no consideration to diminishing tax-paying ability caused by the support of dependents, it is unfamiliar to the Japanese individual income tax system. In addition, since exemption and other income exemption are instituted in mixture, the system will be more complex.

b. Exemptions and Deductions for Elderly

At present, various measures have been introduced to elderly people, including special additional exemptions for old-age person (provided that income of a elderly taxpayer is ¥10 million or less) and deduction for

public pension. Meanwhile, "Revising the System of Specially Treating Aged Persons" has come up as one of the subjects in the Broad Outline of Aged Society (Cabinet Decision of December 2001).

Amid the falling birthrate and aging population, it is urgent to revise exemptions for middle-aged and elderly persons and to ensure fairness between elderly people and working people who support the social security system. According to an OECD study, Japan's ratio of tax amounts to social security benefits is extremely low. Thus, taxation at public pensions and benefits according to the capacity of aged persons will contribute to adjustment of actual benefit levels, resulting in fairness between generations as well as among aged people.

Regardless of the fact that a taxpayer can deduct public pension premiums at full amount in the form of deduction for social insurance premium, deduction for public pension is given at the time of receiving pension benefits. In other words, public pensions are virtually exempt from taxation at the stage of both contribution and payment. In addition, both deduction for employment income and deduction for public pension income are applied to those who have employment income and public pension income.

From the standpoints mentioned above, requirements for exemption for elderly should be revised so that the exemption is applied to the elderly truly in need of it. Deduction for public pension is, in principle, supposed unnecessary because deduction for social security premium is applied at the time of making contribution. Meanwhile, as a minimum, from the standpoint of promoting fairness among generations, the relationship between additional exemption and old-age pension should be reviewed so that these exemptions can be reduced substantially.

Furthermore, the scope of deduction for social insurance premium must be reviewed because the pension system has been diversified and a number of contributions included in the scope are optional.

c. Deductions for Salary and Retirement Income

A. The total deduction for employment income or ¥62.8 trillion accounted for some 30% of the gross employment income of ¥222.8 trillion (FY 2002 budget basis) at macro level. The ratio is regarded as quite high and not legitimate as the standard deduction for expenses necessary for employment income earners. Most of the major advanced nations are adopting a fixed amount allowance as the standard deduction, or define the deduction limit. Compared with these deductions, Japan's deduction is high and has a problem of having no upper limit of deduction.

The Tax Commission has regarded that the characteristics of deduction of employment income cover two elements, that is "standard deduction of working expenses" and "special consideration for the situation of employees, and make adjustment to other types of income". The number of employees accounted for some 80% of the working people in 2001. Increasing number of workers are selecting various types or work style. Under these circumstances, paying special consideration to conditions of employees is becoming less necessary.

In conclusion, deduction for employment income should be reduced by seeking for a reasonable level of standard deduction for working expenses.

Employees are of the view that business proprietors could manipulate their income to reduce tax burden by attributing income to their corporation and that their income is not monitored well. This

view is leading to the feeling of bearing unfair tax burdens among employees. Thus, in reducing deduction for employment income, how to eliminate such feeling of inequity must also be taken into consideration.

The deduction for specific expense has been instituted as the mechanism to allow deduction of certain types of actual expenses incurred directly and necessary for the working of the employee. However, applications of this system are very limited. When deduction levels for employment income are lowered, an increasing number of employed taxpayers are likely to choose the deduction for specific expense in the future. Although the scope of the Japanese deduction for specific expense is not narrow compared with the scope of major advanced nations, the scope needs a renewed examination to meet changes in socioeconomic conditions.

B. Payments of lump-sum retirement severance vary from corporation to corporation. Nevertheless, deduction for retirement income is calculated simply according to the number of years serving for the company. In addition, the calculation of retirement income is not necessarily reasonable. For example, tax is imposed on a half of employment income even if the number of years serving for the company is short. In particular, when the number of years serving for the company exceeds 20 years, deduction amount for retirement deduction increases to ¥700,000 per year from ¥400,000 according to the present retirement deduction system.

Employment patterns and practices in Japan have been changing in recent years. Such changes include early retirement, job change, change in the method of paying retirement severance and payment in

the form of larger salary with no retirement severance.

From the standpoint of ensuring fair and neutral taxation, taxation at retirement severance should be revised by examining actual situations of working conditions and retirement severances.

d. Exemptions/Deductions as Special Taxation Measures

Deductions for life insurance, non-life insurance, home loan, etc. have been instituted in order to fulfill particular policy objectives. On the other hand, however, they have distorted the tax system and create “hollowing out” (shrinking tax base and revenue) to some extent.

Since it is intended to conduct review on fundamental items of income tax such as personal exemptions with a view to streamline and abolish from the viewpoints of expanding income tax base, exemptions and deductions given as special taxation measures should be examined more rigorously and reviewed with a view to abolish them.

(3) Individual Inhabitant Tax (local tax)

a. Basic Policy

Individual inhabitant tax is characterized as having proper features that costs for the local community should be borne by as many local people as possible according to their capacity and that local taxpayers can clearly recognize the relation of burden-to-benefit for receiving social welfare and other man-to-man services that the local government provides for local people under the situation of the falling birthrate and aging population. Individual inhabitant tax is also regarded as hardly having partial taxation sources and therefore its tax revenue is stable. Thus, individual inhabitant tax should be upgraded and consolidated as main local tax.

b. Taxation on Income Basis

Exemptions and tax threshold of local inhabitant tax should be set to a

level lower than income tax since as many local taxpayers as possible should bear burden due to the recognition of the relation of burden-to-benefit in the tax

c. Taxation on per capita basis

The per capita levy has been revised for several times so far. However, the tax rate of capitation still remains low when compared with changes in national income.

Thus, the gap of per capita levy and their level should be reduced and revised according to brackets of population phase.

The non-taxation measure on the wife of a co-living taxpayer should also be revised from the standpoint of individual-based taxation along with the development of gender-equal society.

2. Taxation of Corporations

1) Corporation Tax

(1) Present Situation and Challenges of Corporation tax – Revenue raising and vitalization of socioeconomy -

Repeated reductions of corporation tax and falls of corporate revenues in recent years have led to a drastic fall of corporation tax revenues. As a result, corporation tax revenue now accounts for a little more than 20% of national tax revenues. In addition, some 70% of corporations in Japan are operating at a deficit.

However, corporate activities are increasingly expected to expand worldwide. Under these circumstances and from the standpoint of vitalizing the socioeconomy, reforming corporation tax has come up as a challenging subject while ensuring the revenue raising function of corporation tax.

(2) Directions of the Reform in the Future

a. Basic policies - Instituting a less-distorted and neutral tax system and prioritize special taxation measures -

The corporation tax system should be compatible with international standards as well as impartial and neutral for business activities in order to respect inventive activities of corporations so that corporation can maintain and strengthen their competitiveness.

From these standpoints, the Japanese corporation tax system has undergone a number of reforms since FY 1998. For example, the corporation tax rate was reduced to the internationally compatible level while the taxation base was expanded. In addition, the consolidated tax payment system was introduced. These corporation tax reforms must be strengthened and maintained in order to vitalize the socioeconomy.

Meanwhile, Japan's corporation tax rate (national) is at the same level of major advanced nations as a result of reductions of corporation tax rate. Further reduction of corporation tax rate by taking into account of the levels of corporation tax in developing countries is inappropriate.

Instead, the level of Japanese corporation tax rate should be examined and revised by considering the level of entire tax burdens, the entire tax scheme and the balance of tax rates of other advanced nations.

When taxation by the size of business is introduced into enterprise tax (local tax) on corporation, the effective tax rate on corporate income will be reduced.

Meanwhile, existing special taxation measures must be consolidated and streamlined drastically in order to promote simplified taxation and expand the taxation base. At the same time, truly effective measures must be implemented in a targeted and prioritized fashion to reform and

vitalize the socioeconomy. In line with these reforms, problems on corporation tax must be worked on in response to new moves in the socioeconomy, including emerging diverse business operations.

b. Targeting of Tax Incentives – Prioritize tax incentives based on a clear national strategy -

In order to strengthen the competitiveness of Japanese corporations and reform the present industrial structure, Japan has to focus on important areas, including regulatory reform and expenditure cut, based on a clear national strategy in anticipation of industry and technology that will lead the 21st century. In the area of tax system, on the one hand, rationalize and streamline existing special tax measures, on the other hand, special tax measures must be targeted and prioritized in the truly effective areas such as R&D.

c. Reappointing new socioeconomy Trends

Diverse investment forms have emerged along with globalization of economic activities and financial deregulation. In line with these moves, business forms and scales of corporation have changed. In society with a falling birthrate and aging population, non-profit making activities by NPO corporations are expected to play a greater role in building a vital socioeconomy.

In response to these new moves, the following subjects should be worked on depending on the type of corporation (see the appendix):

A. Taxation at retained earnings of family corporations, taxation of partnerships and other different business entities should be examined from the standpoint of ensuring appropriate taxation and promoting smooth activities of corporations.

B. Taxation of non-profit making corporations should be examined

comprehensively. Specifically, taxation at profit-earning business of corporations in public interest and reduced tax rate of corporations in public interest and associations/cooperatives should be examined by considering moves of reforms of corporations in public interest. In addition, taxation at NPO corporations, non-profit mutual benefit corporation and other new forms of corporations should be examined.

C. Taxation of donation should be examined by taking into account of tax treatment adopted in other countries and the activities of non-profit making activities. Relations with various systems, including the certified NPO corporation system should be considered as well. Such examinations should be made so that NPO corporations can have smooth operations as new leaders for the public welfare.

2) Enterprise Tax (local tax) - Introduction of Taxation by the Size of Business -

The introduction of assessment of enterprise tax of corporations by the size of their business is an important reform for ensuring fair distribution of tax burden, clarifying the characteristics of tax as a benefit-based taxation, stabilizing main local tax that support decentralization, vitalizing the Japanese economy, and promoting economic structural reforms. The introduction of pro forma standard will come to correct "hollowing out of taxation" (shrinking tax base and revenue) - or the problem that some 70% of corporations bear no enterprise tax on corporation - and establish a corporation tax system where profit-earning corporations will be treated in a more appropriate way. Pro forma standard taxation of enterprise tax should be introduced at an early stage in order to promote true decentralization by clarifying the relationship between burden and benefit.

Part III. Consumption Tax

1) Present Situations and Problems of Consumption Tax - for the formation of stable main tax -

Consumption tax was introduced in 1988. Since then, revenues from consumption tax have continued to be stable, accounting for some 20% of national revenues. Thus, consumption tax has been fixed into the taxation system as one of the main taxes in Japan. Meanwhile, some people have an abiding distrust of the current tax system. Consumption tax is expected to play a greater role along with the advancement of falling birthrate, aging population, and globalization. Thus, it is urgent to gain trust in the consumption tax system and to revise the tax rate. It is often pointed out that consumption tax imposes regressive tax burden. This problem must be discussed and judged not only within the consumption tax system but also from the standpoints of the overall economy, including the tax system and the government's expenditures.

2) Directions of Reforms in the Future

(1) Basic policies – the need to gain trust in the tax from general public and to enhance the roles of consumption tax -

Consumption tax plays a quite important role in a society with a falling birthrate and aging population. Consumption tax is neutral to economic activities and does not ask excessive burden on working generations. In addition, the consumption tax system contributes to ensuring fairness among different generations, promoting a vital socioeconomy, and ensuring stable tax revenues.

Since growing social security expenditures and financial structure reforms are anticipated, the rate of consumption tax needs to be raised and its roles need to be enhanced. To these ends, thorough administrative

reforms must be continued. Moreover, a number of measures must be taken in order to gain people's trust in the consumption tax system and review the taxation into a highly transparent and fair tax system.

From the standpoints mentioned above, the revision will be made on special treatment and the number of filing and tax payment times for the SMEs (small and medium size businesses). In addition, concerted efforts should be made to avoid delinquency of consumption tax payment and efforts should be made to collect the unpaid consumption tax. The competent administrative authorities should also urge vendors/suppliers to adopt total price indication system (including of tax and price of goods and services) for convenience of consumers.

(2) Reforms for Improved Reliability and Transparency – Fundamental review of preferential treatments for SMEs -

a. Preferential Systems for Small- and Medium-Businesses

Preferential systems for small- and medium-business operators have been instituted in order to simplify and relieve their clerical burden. Nearly 13 years have passed since the systems were introduced. In order to gain people's trust in the tax system and improve the transparency of the tax system, urgent and thorough efforts should be exerted for the examination and revision of the preferential systems.

A. Tax Exempt Threshold

Tax-exempt threshold for consumption tax (the amount of taxable sale must be ¥30 million or less) has been left unchanged since the preferential system was introduced. At present, more than 60% of business operators fall into exempt enterprises. This has raised the suspicion of many consumers that the amount equivalent to the consumption tax paid by consumers may not be paid to the national

treasury. This seems one of the major factors that many consumers distrust consumption tax.

Therefore, the present level tax exemption threshold should be scaled down drastically in consideration of different clerical capacities of individual business operators and corporations.

Under the present tax exemption threshold system, since many exempt enterprises have transactions with other business operators, credit for consumption tax amount on input from exempt enterprises has been granted. As a result, transparency of the consumption tax system is damaged. Therefore, the tax exemption limit system for business operators should be scaled down drastically to cover this damage before examining the introduction of an invoice system, which is described later in this report.

B. Simplified Tax System of Consumption Tax

The simplified tax system (translator's note: Vendors/suppliers with taxable sales of less than Y200 million during the base period can elect to use "deemed input ratios" designated in accordance to the types of businesses) has been revised in the past, and its application has been on the decrease. However, the consumption tax system has taken root in society. Business operators seem to have become familiar with tax payment deskwork. It is also pointed out that in order to pay less tax, an increasing number of small- and medium-business operators with deskwork capability have been applying for the simplified tax system after calculating the amount of their tax that they are supposed to pay. Therefore, the simplified tax system should be revised drastically, including the discontinuance.

b. Self-Assessment and Payment System

Considering that the characteristics of the consumption tax are similar to that of deposit by consumers, the frequency of the consumption tax self-assessment and payment system has been revised in the past in order to solve the problem that consumption tax paid to business operators is used for their fund operations. When considering this characteristic of consumption tax, the number of self-assessment and payment times should be increased. When the number of self-assessment and payment times are examined, clerical burden of taxpayers, tax administration cost and delayed payment of consumption tax must also be taken into consideration.

c. Total Price Indication System (method of displaying prices for consumers)

More positive efforts should be made to discuss displaying the total price, including consumption tax, of commodities for the convenience of consumers (total price indication system). As is seen in many European nations, the total price indication system should be promoted by relevant government agencies in consumer protection administration as soon as possible.

d. Invoice System

Adoption of an "invoice system" will become a subject for examination in order to improve taxpayers' trust in the consumption tax system. The invoice system requires that business operators should keep copies of (tax) invoice for crediting consumption tax on input. However, the (ordinary) bill keeping system under the present consumption tax system has no particular problem in crediting appropriate amount of input tax under the single tax rate and the narrow

nontaxable scope. In the future when multiple tax rates are introduced, adoption of the (tax) invoice system should be examined more specifically, including the scope of reduced tax rates.

(3) Tax Rate Structure of the Consumption Tax

A single tax rate is most desirable for consumption tax from the standpoints of simplified taxation and neutral position to economic activities. If the consumption tax rate should be raised to a double-digit percentage in the future in Japan as in European countries, consumption tax on foods etc., should be lowered in order to relieve regressive characteristics of consumption tax burden on income. In this case, however, the scope where such lowered consumption tax is applicable should be limited to minimum by considering socioeconomic costs, including clerical burden of vendors/suppliers concerned.

Expansion of the scope of exempt transactions and adoption of zero-rating are not desirable because these measures will severely spoil the characteristic of consumption tax that consumption should bear fair tax as broad as possible.

(4) Local Consumption Tax

Local consumption tax was legislated by tax reform for FY 1994 and has been enforced since FY 1997 mainly for the purposes of promoting decentralization and upgrading local welfare. Revenue from local consumption tax is less maldistributed among local government through clearing and now plays an important role as a stable main local tax. Along with falling birthrate and aging population, local consumption tax will have to play a greater role to serve welfare, education, and other social needs in local administration. Thus, local consumption tax must be upgraded and consolidated in the future.

Part IV. Property Taxation and other taxation

1) Inheritance Tax and Gift Tax

(1) Basic Policies for Reform - Meeting structural changes of socioeconomy and appropriate tax burden -

Conditions surrounding inheritance tax have been changing greatly due to the following factors:

1. Transfer of assets through inheritance is expected to increase due to the growing stock economy.
2. The role of public burden in supporting elderly people is increasing as the social security system has been upgraded. Thus, a part of individual assets of deceased person should be resolved into society.
3. The role of inheritance assets has become relatively less significant to form the economic base of inheritors because inheritors' asset acquisition through inheritance tends to take place in their latter part of life of children as the life expectancies is getting longer.

Under this circumstance, contribution of a broader scope of appropriate burden to the society would be required.

In such a case, on the one hand, the maximum tax rate must be lowered from the standpoint of appropriate tax burden; on the other hand, the degree of present progressive tax rates structure should be kept.

Japan's gift tax is based on single calendar year taxation. Gift tax burden is set to relatively higher level from the standpoint of preventing potential inheritors from avoiding inheritance tax payment. Transfer of assets to inheritors through inheritance tends to take place in their latter part of life because of the long-living ancestor. Therefore, ensuring the neutrality of taxation effect on the timing of asset transfer is becoming important.

If assets owned by ancestors (financial assets and real assets including

houses) are transferred to their inheritors at the time earlier than the actual death of the ancestors, the transferred assets may be used more usefully by younger generations and thus, it is hoped to contribute to vitalization of the socioeconomy. From these standpoints, how to adjust inheritance tax and gift tax (smooth transfer of assets from parents to their children while they are living) should be examined.

Special treatment related to succession of business contributes to smooth inheritance of SMEs. However, excessive incentives for business inheritance after succession could lose the balance with new formations of the business and new business deployment. Thus, special measures on business inheritance should be carefully examined.

In this case, since the period that an inheritor works with the ancestor for the business tends to become quite long, it is important to promote smooth transfer of business during life and to consider the inheritor's contribution to the formation of the ancestor's assets.

(2) Directions of Inheritance Tax Reform

a. Tax Base

Basic exemption should be lowered from the standpoint of Basic Policies for reform (above) and plunged land prices. In the adjustment of inheritance tax and gift tax, relation with basic exemption for gift tax should be reexamined for revision.

Non-taxation measure for death benefit (of life insurance) and retirement deduction at death should be scaled down or discontinued by taking the improved public social security system into consideration from the standpoints of simplified taxation and keeping neutral to asset selection.

Special treatments related to business succession, including the special

treatment for small-scale houses, should be examined by taking dropping of land prices for a long period into consideration. The examination should include possible reorganization of the present special treatments into a special treatment for entire business assets in the future.

b. Tax Rate Structure

The maximum tax rate of inheritance tax (50%) is much higher than that of income tax. It is considerably high compared with maximum tax rates of other countries too. Thus, it is appropriate to lower the maximum tax rate of inheritance tax.

However, the degree of present progressive taxation should be maintained by considering "Basic Policies for reform" and considerable relief of burden of rich asset holders due to the lowering maximum tax rate on inheritance tax.

Tax rate brackets should be gradual, depending on the amount of inheritance, since sharp changes in tax rates are inappropriate because inheritance is extraordinary and accidental.

(3) Directions of Gift Tax in the Future

a. Integration of Inheritance Tax and Gift Tax (move from gift taxation on annual gifts to gift taxation on accumulated gift basis)

In the advancement of the aging society, social request for gift during life has been deep-seated. From this standpoint, possible integration of gift tax with inheritance tax should be examined, including accumulative taxation (see the appendix).

Methods for accumulative taxation are mainly divided into lifetime accumulative taxation and fixed period accumulative taxation. In the both methods, the taxpayer and tax administration are need to keep record of assets concerned for long time. Therefore, in order to ensure

appropriate enforcement, if taxation of gifts on accumulative basis is to be introduced, tax compliance measures to record, identify, match information for a long time of period need to be introduced. This will include introduction of automated/computerized systems in tax administration, examination of shift of burden of proof and the extension of period of limitation of tax audit, and introduction of TINs.

Until the above-mentioned management systems are prepared, neither types accumulative taxations can be enforced comprehensively. Due consideration should be given to the degree of need for allowing gift from parents to their children while they are living, and the situation of assets by the Japanese people, and the possible mechanisms for the accumulative taxations must be examined. Along with further discussion for this, introduction of a preliminary measure for gift tax should be examined from the standpoint of respecting the position of keeping neutral to choosing the time of asset transfer to the next generation.

In examining the possible integration of inheritance tax and gift tax and the preliminary measure, sufficient compliance measures should be taken to eliminate the possibilities that rich asset holders may be triggered to plan tax avoidance and that taxation administration may omit proper taxation due to difficulties in taxation execution because managing gifted assets will last for a long period of time.

b. Treatment of Gift to a Third Party

Tax treatment of gift to a third party who is not a legal inheritor is also being discussed. In this case, the gift could be treated as income of the third party by examining the real condition of the gift. Such income taxation will contribute to preventing inheritance tax avoidance.

2) Property Tax (local tax)

(1) Present Situations and Challenges of Property Tax

Taxable bases of property tax are fixed property (immovable property) and equipment which exist in any municipalities. Since the allocation of tax basis of property tax is less impartial, it is an appropriate main tax for local municipalities. Thus, revenues from this tax must be stabilized.

(2) Directions of Reform in the Future

It is appropriate that the assessment standard that aims at 70% of public announcement prices of land is maintained from the standpoints of nationwide assessment equation and appropriateness.

Equalization of burden levels has been making progress since FY 1997 to some extent although a lot of unlevelled areas are still found in many parts of the country. Thus, additional measures to promote equalization and appropriateness of burden level must be taken by observing trends in revision of assessments, situation of burden levels, and fiscal conditions of local governments.

3) Taxation of Land and Housing

The land tax system has been revised according to changes in land prices. Most of the taxation measures strengthened and introduced in the bubble economy period were discontinued or abolished and returned to the level before the bubbled economy.

At present, land prices are bi-polarized and individualized. Thus, land prices must be analyzed not only from the standpoint of adjustment period after the bubble economy but also from the standpoints of trends in local economies and changes of industrial structure. Under the structural changes, the entire land policies are required for revision, including the positioning of the basic policy of the Basic Law of Land.

In line with the revision of land policies, the land tax system needs examination by considering changes in land prices and the fact that the taxation base for the income of land transfer has been eroded greatly.

From special policy purpose, various tax reduction measures have been instituted for an owner-occupied home at the levels of acquiring, holding and transferring of the home. However, the rate of owner occupied house has reached a certain high level. With advancement of falling birthrate and aging population, demand for homes is expected to decrease. On the other hand, demand for leased houses and changing homes will increase. Thus, housing policies centering on promoting acquisition of one's own homes must be re-examined. Under these changing circumstances, tax reduction measures, such as deduction for home loans, should be re-examined.

4) Taxation of Financial Assets

Taxation at income from financial assets will come to play a greater role in the future. This is because earned income is expected to decrease relatively while the stock economy (progressively increasing financial assets) and aging population continue to grow and the birthrate continues to fall. In the meantime the shift from deposit savings to investment by the households are being promoted.

Under the circumstances mentioned above, the current financial tax system should be reexamined in aiming to ensure the neutral position among financial products, to keep fair taxation at income in other than financial areas, and to promote simplified taxation. In line with the examination, due attention should be paid to the characteristics of diverse and complicated financial assets, globalization and computerization of the financial market, geographically mobile nature of the asset, and relations of taxation at entities (collective investment schemes). In this case, the

taxpayer identification number system and other income measures for monitoring income should also be discussed for consolidation.

In addition, the idea of "dual income tax" and the unification of tax on financial assets should be examined in considering relations to transferring to comprehensive income taxation and the balance of taxations of capital income and labor income. (see the appendix).

Part V. Others

1) Liquor Tax and Tobacco Tax

Like many other countries, Japan has been taxing liquors and tobaccos as special articles of taste at tax rates higher than on other goods. Thus, liquor tax and tobacco tax have played an important role in the Japanese tax system. When taking the severe financial conditions of the government into consideration, appropriate tax burden levels should be continued in the future by considering their production and consumption levels of liquor and tobacco.

(1) Liquor Tax

From the standpoints of ensuring the neutral and fair position in tax system, the present classification of liquors (10 types) should be simplified to narrow gaps of tax burdens among different types of liquors. In particular, liquors in the classifications that are inconsistent with the basic principle of the "same burden on the same type of liquors" should be re-classified in order to balance burdens among liquors.

(2) Tobacco Tax

The US and many other European nations have raised tobacco tax in recent years.

By considering the rate of tax to the retail price of tobacco, consumer

trends, trends in other nations and fiscal conditions of the government, raising the tax rate of tobacco should be examined.

2) Earmarked Revenues and Energy-Related Taxes

Gasoline excise and oil tax are earmarked for certain purposes. Earmarked revenues are used when the benefit and burden of specific public service are closely related and when the financial source of the service must be ensured. Although earmarked revenues are useful in ensuring the source of finance systematically, the mechanism could lead to an inappropriate distribution of financial resources, contributing to a congealed budget structure. Thus, the mechanism of applying earmarked revenues must be constantly examined.

The basic mechanism of the earmarked road revenues, including their expenditures, should be examined by considering the original purpose and historical background of the system. Specifically, it should be examined whether such earmarked revenues should need to be maintained for road construction and whether the earmarked revenues have not contributed to the congealed budget system. The Tax Commission is of the opinion that the earmarked road revenues should be reexamined for revision, including re-classification into general account revenues, although some of the members of the committee are of the opinion that the revenues should be maintained as they are.

Concerning Japan's energy-related taxes including the earmarked road revenues, the entire tax burden on automobiles is not so high in Japan seeing from international levels. Thus, lowering tax burden on automobiles is inappropriate considering social costs of automobiles and for environmental preservation. It is also pointed out that the present automobile-related tax items are too many and complicated. Discussions

should be continued on an appropriate tax system relating to automobiles.

3) Response to Environmental Issues

The Guidelines for Promoting Measures against Global Warming was reviewed in March 2002 for the purpose of attaining Japan's goals set forth in the Kyoto Protocol. This broad outline also states that "continuous and comprehensive examinations should be made on tax, charge, and other economic methods by comparing with other methods." It is advisable that the government should work on environmental issues based on people's understanding and support because the issues will eventually ask people to bear financial burdens in the form of tax. In this case, the tax system should have concrete positioning in environmental policies of the national and local governments based on the Polluter-Pays Principle (PPP). In addition, relations with existing energy related taxes should be examined for revision.

4) International Taxation

Along with the development of globalization, and computerization, tracing diverse corporate activities becomes increasingly difficult. An increasing number of corporations have been trying to reduce taxable income with intention in the form of arbitrage transactions where international differences of tax systems and their gaps are used. In international taxation, outflow of income from the nation virtually means to lose the taxation right. Therefore, the taxation system relating to activities beyond the national boundary should be revised in order to ensure Japan's taxation right on cross-border activities. In addition, enforcing appropriate international taxation must be carried out from the standpoint of keeping the fair and neutral position to domestic and cross-border economic activities.

More specifically, in response to diverse formations of overseas-affiliated corporations in Japan, taxation at diverse business entities and Japanese branches of foreign corporations should be examined for revision. Meanwhile, in anticipation of activities of Japanese corporations beyond the national border, examinations should be continued on consolidation of foreign subsidiaries and rationalization of the foreign tax credit system. In addition, from the standpoint of ensuring appropriate tax enforcement that meets globalization, it is important to improve access to overseas information sources through exchanges of information with competent tax authorities of foreign governments based on tax treaties and other treaties with those governments. For a precondition of such access, legal systems concerned should be introduced so that the competent authorities of the Japanese government can provide information requested by a foreign government with which Japan has concluded a tax treaty (see appendix).

Electronic commerce is global by nature and thus its problems cannot be dealt with unilaterally. Through discussions at OECD, an internationally concerted action in this area should be examined and through which, foreseeability of business should be improved and appropriate taxation should be ensured.

5) Tax autonomy of local governments

From the standpoint of decentralization, it is desirable for local governments to try to set up their financial sources by utilizing self-determined taxation right. In this case, however, issues relating to taxpayers and base of taxation should be discussed well according to principles of taxation, including fair and neutral taxation. In other words, local governments have to face local taxpayers to implement their taxation

measures at their burden and responsibility.

Part VI. Infrastructure Building to Ensure Taxpayer Trust

In working on the reform of the entire tax systems, it is essential to gain trust of taxpayers in the tax system and tax administration in order to institute a desirable tax system. To this end, tax administration needs to arrange the environment so that taxpayers can carry out self-assessment and tax payment with no difficulty and to consolidate the tax administration system for fair and appropriate taxation. Therefore, to materialize these standpoints, following systems and measures need to be advanced:

1) Taxpayer Identification Numbers (TINs)

Globalization, informatization, and computerization have been prevailing in worldwide economic transactions in recent years. Under this situation, the environments around the taxpayer identification number system are drastically changing. A growing number of Japanese people have also begun to think that the introduction of the system would be inevitable.

In the past, a variety of discussions have been made on the taxpayer identification number system, including the significance of the system, concrete application of the system and privacy protection. Thus, it is urgent to start examination and formulate a concrete scheme for introduction.

2) Withholding and Year-End Adjustment of Income Tax

Income tax is based on taxpayers' self-assessment, and their voluntary filing of returns and payment. And tax withholding and year-end adjustment are carried out on payments of tax on employment income. Since tax amount, including exemptions/deductions as special taxation measures, is adjusted at the end of the year, ordinary employment income earners need no filing an income tax return.

Tax withholding and year-end adjustment should basically be maintained in the future in order to ensure appropriate and reliable taxation and provide the simplified and to provide taxpayers with convenient tax payment system. However, it is also important for employment income earners to file an income tax return by themselves because this will enhance the awareness of bearing common social costs. Thus, examination should be continued on promoting environments for simplified filing system (including electric filing of returns), while paying sufficient consideration to tax administration.

3) Publication of High-Paying Taxpayers

The present public notification system exists in income tax, corporation tax and inheritance tax. It has been playing the role of checking taxpayers with the public since 1950 when introduced for the first time. The public notification system of income tax was modified into the tax amount notification system in 1983 partly for the purpose of honoring high-income taxpayers. The system has been occasionally utilized for a purpose other than the original purposes, posing a concern about possible disturbance of privacy. Meanwhile, it is undesirable that the modification of the system leads to lowered reliability of the self-assessment and payment system. Thus, discussions should be made on the existing public notification system, including introduction of an alternative system, by paying attention to the significance that high-income taxpayers should be honored by society.

4) Others

- (1) It is necessary to accomplish smooth introduction of electric filing of tax return and electric tax payment through the Internet in addition to the conventional paper filing system in order to improve the utility of taxpayers by seizing computerisation and digitalization. Due

consideration should be given to how to ensure security.

(2) It is important to enhance tax information reporting system based on people's understanding and support in response to structural changes of the socioeconomy including internationalization and informatization. This will contribute to the realization of fair and appropriate taxation.

(3) It is also important to work on the tax administration for better arrangement and the promotion of fair and appropriate taxation. These include promotions of easy-to-understand tax PR, quick and accurate response and answer to questions of taxpayers, and execution of accurate investigation and guidance.