JTAX

JAPAN TAX GROUP

JTAX | GUIDE TO SETTING UP A KABUSHIKI KAISHA ("KK") IN JAPAN

YOUR TRUSTED PARTNER
in Japan

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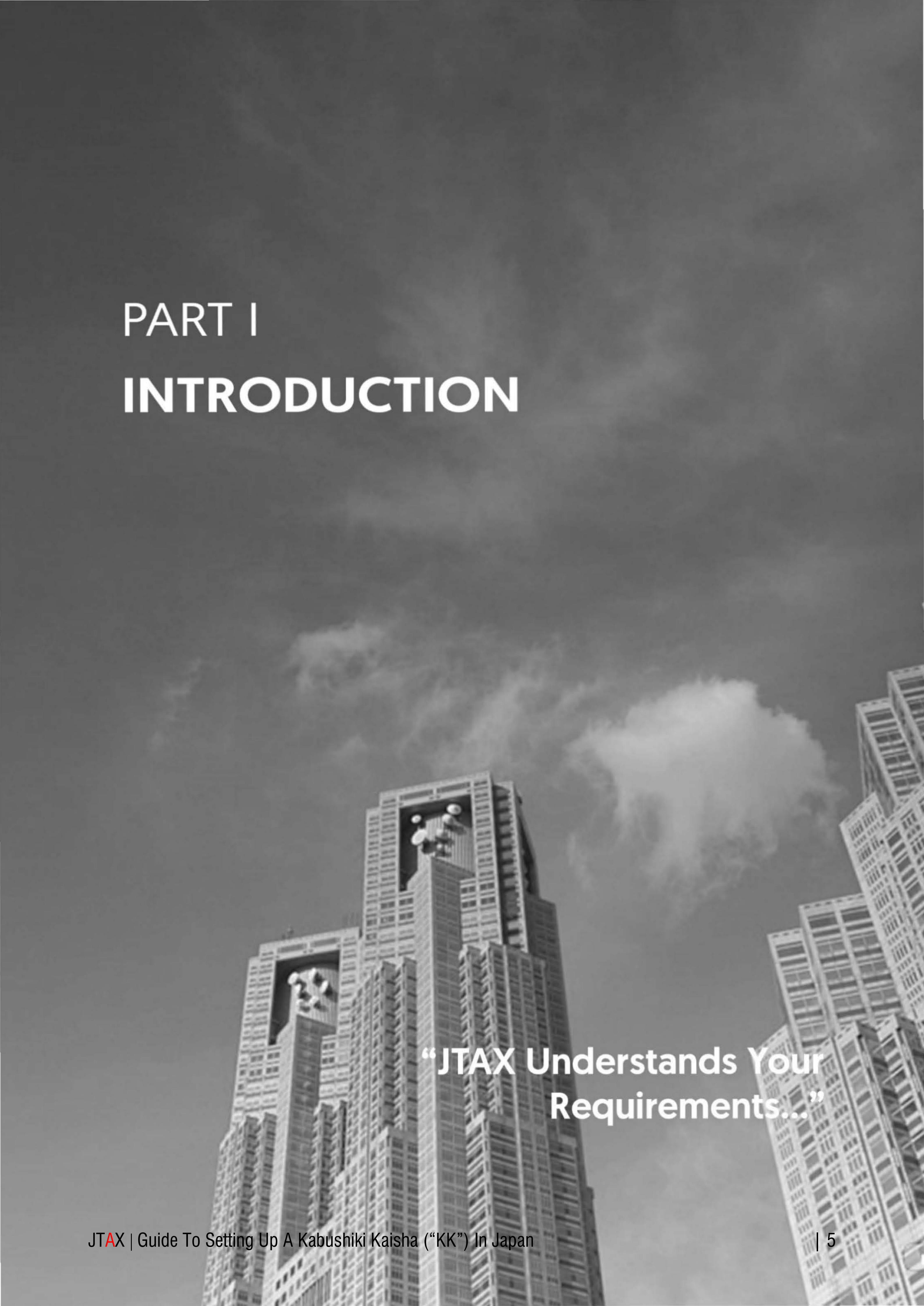


ABOUT JTAX

JTAX is a member of the Accounting Asia Group, a leader in Asia focused professional services.

Tracing its roots to 2001, JTAX's team of Japanese and foreign professionals has assisted hundreds of foreign clients to establish and run their businesses in Japan. Our management is drawn from the Big 4 and has extensive experience responding to the requirements of clients ranging in size from listed multinationals to start-ups.

JTAX recognizes the practical difficulties associated with operating a business in Japan and our aim is to provide clients with one-stop assistance. Our team therefore provides a comprehensive range of services including tax advisory, tax compliance, incorporation, accounting, cash management / expense payment, payroll / HR, Japan resident nominee directors, and work visas. In addition to the convenience of dealing with a single service provider, JTAX ensures that its services are handled in a coordinated manner. For example, Japan work visas may be dependent on having a properly incorporated company and an appropriate tax structure, etc.

In addition to working directly with clients, JTAX is also able to assist foreign law firms and accounting firms whose clients require assistance in Japan.

Please Contact Us for more information about any of our services.

JTAX MANAGEMENT

Dean Page – Administrative Partner

Dean Page is JTAX's administrative partner. He is a leading expert on Japanese and international tax and on doing business in Japan.

Dean worked for seven years in the Big 4, most recently as a partner at Ernst & Young (E&Y). At E&Y he served as the inbound account leader in which role he had responsibility for overseeing the delivery of services to E&Y Japan's foreign clients.

At PricewaterhouseCoopers ("PwC") Dean headed the Pathfinder Group, a team that specializes in assisting foreign clients to establish operations in Japan.

Since 2001, Dean has co-headed the International Tax Education Program (ITEP) and acted as an Adjunct Professor at the Beasley School of Law, Temple University, Japan Campus. He is the author of numerous articles related to Japanese and international tax.

Dean is admitted as both an attorney (England / Wales) and as a CPA (USA, California).

JTAX SERVICES

JTAX recognizes the practical difficulties associated with operating a business in Japan and our aim is to provide clients with *one-stop assistance*. JTAX key services include

- Tax Consulting and Compliance
- Tax Services
- Accounting & Bookkeeping
- Bank Account Management & Expense Payment
- Payroll & HR
- Japan Work Visas
- Japan Incorporations
- Japan Nominee Directors
- Japan Registered Address & Virtual Office Solutions
- Due Diligence & Deal Integration Services
- Outsourcing Solutions including Finance, Tax, Accounting, and Payroll & HR
- Real Estate Advisory Services

Please Contact Us for more information about any of our services.

PART II

JTAX JAPAN INCORPORATION SERVICE

"JTAX Understands Your Requirements..."

1. Introduction to JTAX Japan Incorporation Service

a. Overview

JTAX can assist its clients in the establishment of a wide range of entities in Japan.

Our main work in this area is helping clients establish:

- Incorporated Entities / Subsidiaries
  - Kabushiki Kaisha ("KK").
  - Godo Kaisha ("GK").
- Japan Branches of Foreign Companies in Japan.
- Japan Representative Office of Foreign Company / Japan Liaison Office of Foreign Companies.

The focus of this brochure is to provide clients with information regarding setting up a Kabushiki Kaisha ("KK") in Japan.

Please contact us if you would like more information about other types of entity including Godo Kaisha ("GK"), Japan Branches of Foreign Companies, or Japan Representative Offices of Foreign Company / Japan Liaison Office of Foreign Companies.

b. JTAX Kabushiki Kaisha ("KK") Incorporation Service

JTAX's key Kabushiki Kaisha ("KK") incorporation capabilities include:

- Initial consulting to assist clients to ensure that a Kabushiki Kaisha ("KK) is appropriate to their needs.
- Provision of Japan nominee directors for the new Kabushiki Kaisha ("KK") to ensure a smooth incorporation, improve internal control in Japan, and limit director compensation deductibility issues.
- Provision of a legal registered address for the Kabushiki Kaisha ("KK") in Japan.
- Assistance with serviced offices and virtual offices.
- Registration of a new Kabushiki Kaisha ("KK")
- Assistance with post incorporation issues including initial tax filings.
- Outsourcing services to handle ongoing key functions in Japan including tax, accounting, payroll, etc.

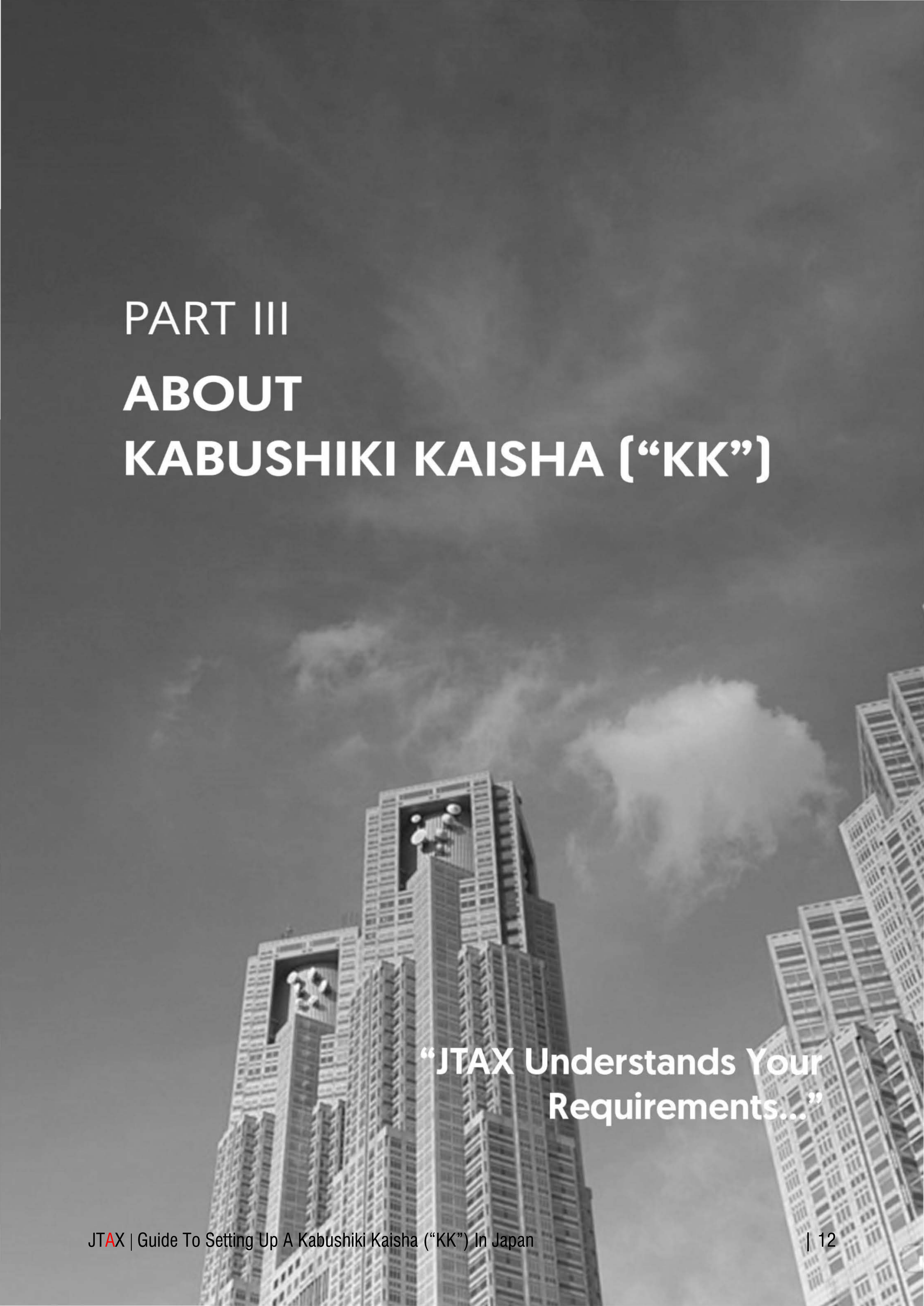
2. Why Should We Set Up a Company In Japan?

Common reasons to incorporate in Japan include:

- Japan is the world's third largest economy. Incorporating a company in Japan will help you to take advantage of an unparalleled market opportunity.
- Japan is a difficult market to exploit without a solid presence on the ground. Potential Japanese customers and partners will have more confidence in your ability to deliver if you operate via a Japanese company.
- In order to employ top quality people, it is vital to have a local Japanese entity. If you do not have a local entity, potential Japanese employees will perceive that you lack commitment to the market. It is generally not possible to offer regular employee benefits if there is no Japan entity.

PART III

ABOUT KABUSHIKI KAISHA ("KK")



"JTAX Understands Your Requirements..."

1. Introduction

Kabushiki Kaisha ("KK") is a type of business corporation defined under Japanese law. The Kabushiki Kaisha ("KK") is a very well-known form of doing business in Japan with the first Kabushiki Kaisha ("KK") having been established in 1873. Due to this long history, the Kabushiki Kaisha ("KK") has historically been the form of business most often utilized by foreign companies in Japan.

A Kabushiki Kaisha ("KK") is seen as presenting a strong commercial image and in certain industries from a practical viewpoint it may not be possible to do business in any form other than a Kabushiki Kaisha ("KK"). Certain licenses may only be available to a Kabushiki Kaisha ("KK").

The most recent major changes to the law concerning Kabushiki Kaisha ("KK") (the Commercial Code and new Company Law) took effect on 1 May 2006. These changes allow for single director Kabushiki Kaisha ("KK") and also eliminate the previous requirement that Kabushiki Kaisha ("KK") be established with a minimum of JPY10 million in paid in capital.

Effective 1 April 2015 the *legal* requirement for a Japan resident director was removed (but see further comment on this issue below.)

2. Corporate Designator

a. In Japanese

While *Kabushiki Kaisha* is most commonly used as a post nominal (e.g., JTAX Kabushiki Kaisha) it can also be used as a pre-nominal (e.g., Kabushiki Kaisha JTAX.)

Kabushiki Kaisha is frequently abbreviated as *KK* (e.g., JTAX KK.)

b. English Translation

Kabushiki Kaisha (KK) is typically translated to English as "Co., Ltd." or "Corporation".

So, for example, JTAX Kabushiki Kaisha could be translated as JTAX Co. Ltd. or JTAX Corporation.

"KK's" are sometimes referred to as either Joint Stock Company or Stock Company.

3. Corporate Governance in Kabushki Kaisha ("KK")

The following are some key concepts associated with corporate governance in a Kabushiki Kaisha ("KK"):

a. Directors

A Kabushiki Kaisha ("KK") has directors who are responsible for executing the business on behalf of the Kabushiki Kaisha ("KK").

Directors must be natural persons (i.e., not corporations.)

b. Representative Director

A Kabushiki Kaisha ("KK") is generally required to have at least one Representative Director.

The Representative Director is generally seen as having full power to represent the company with respect to third parties. The Representative Director will be responsible for maintaining the corporate seal.

In the case of a single director Kabushiki Kaisha ("KK") that director will be the Representative Director.

c. Special Note: Residence Requirement for Representative Director

Technically, there is no longer a legal requirement that a Representative Director be resident in Japan.

However, from a practical viewpoint, a Japan resident Representative Director is likely to be a necessity since, in the absence of a Japan resident individual, it will not be possible to open bank accounts, enter leases, etc. As a result, most clients will appoint a Japan resident Nominee Representative Director.

Appointing a Japan resident nominee Executive Manager is also prudent in terms of maintaining internal control within the Japan operation.

A decision to have no Japan resident Representative Director should be carefully considered since it may make doing business in Japan difficult (if not impossible,)

d. Board of Directors

While it is possible to form a board of directors this is no longer a requirement. Thus, in order to maximize simplicity, many foreign investors will establish a Kabushiki Kaisha ("KK") with two directors but no board of directors. In such cases one director would be resident in Japan (possible a Japan resident Nominee Representative Director) and one director would be a non-resident appointed by the corporate parent.

e. Shareholders

The shareholders are the owners of the Kabushiki Kaisha ("KK") and may be natural persons or corporations. The initial shareholders contribute paid in capital in exchange for shares.

f. Statutory Auditors

When a Kabushiki Kaisha ("KK") is established with a board of directors, it is a requirement that at least one "Statutory Auditor" be appointed. This is an internal company position and not related to an audit of the financial statements undertaken by an external accounting firm. The role of the statutory auditor is to oversee the management of the company.

In a small Kabushiki Kaisha ("KK") the statutory auditor duties may largely be a formality. In larger companies there may be a requirement to appoint up to three statutory auditors and the statutory auditors are likely to have substantial duties.

A statutory auditor may be any person who is not an employee or director of the Kabushiki Kaisha ("KK").

4. Corporate Officers

Japanese law does not generally specify or require any corporate officer positions. As a result, most Japanese companies are directly managed by the directors. The main legal distinction in the Japanese Commercial Code is between normal directors and representative directors. A representative director generally has full power to represent the company.

However, large Japanese companies may utilize a range of director level titles including the following:

Japanese title	English translation	Comment
Kaicho	Chairman	▪ Usually only one. ▪ In a large company this individual would often be a representative director of the Kabushiki Kaisha ("KK").
Shacho	President	▪ Usually only one. ▪ In a large company this individual would often be a representative director of the Kabushiki Kaisha ("KK").
Fuku-shacho	Executive Vice-president	▪ Usually several in a large company. ▪ These individuals may also be representative directors of the Kabushiki Kaisha ("KK").
Senmu-torishmori-yaku	Senior managing director	▪ Usually several in a large company. ▪ In certain companies (though not typically) these individuals could also be representative directors of the Kabushiki Kaisha ("KK")– otherwise they may be normal directors.
Jomu-torishimari-yaku	Junior managing director	▪ Usually several in a large company. ▪ In certain companies (though not typically) these individuals could also be representative directors of the Kabushiki Kaisha ("KK")– otherwise they may be normal directors.
Torishimari-yaku	Director – Finance & Operations, Director – Information Technology, etc.	▪ Actual job title may depend upon the individuals designated job.

The following should be noted with respect to the above:

- In general, boards of foreign companies (i.e., when a board is utilized) do not make such detailed distinctions in rank.
- Even though the above positions are not technically required, foreign investors should nonetheless be aware such titles exist. Senior Japanese employees hired from other large companies may request to use one of the above titles. In addition, in some situations, a title may be advisable in order to indicate an employee's status and authority to negotiate.

5. Taxation of Kabushiki Kaisha ("KK")

a. Introduction

For Japanese tax purposes, a Kabushiki Kaisha ("KK") is treated as a per se corporation and is subject to Japanese corporate tax on its worldwide profits.

As a result, a Kabushiki Kaisha ("KK") is subject to double taxation (i.e., profits are first taxed at the corporate level and dividends are then taxed in the hands of shareholders.)

b. Contrast Japanese Godo Kaisha ("GK") from a U.S. Perspective

Where United States investors utilize a GK it may be possible for those investors to utilize the Internal Revenue Services "*check-the-box*" rules. This effectively allows the US investors to treat the GK as a branch of the US company (for US tax purposes.). Such treatment is not possible with a Kabushiki Kaisha ("KK"). US investors should therefore consult with their US tax advisors to determine whether a GK would better suit their needs.

c. Other Tax Considerations

It should be borne in mind that methods other than (after tax) dividends that can be employed to distribute Kabushiki Kaisha ("KK") income to foreign investors. This may include royalties, interest (via interco loans) and intercompany service agreements.

Regardless of the manner in which profit is distributed, the role of double taxation agreements ("DTA") need to be considered. DTAs may reduce the amount of withholding tax that is payable when cross border payments of interest, dividends, or royalty are made. The availability of DTA relief will often depend on the residence of the GK investors.

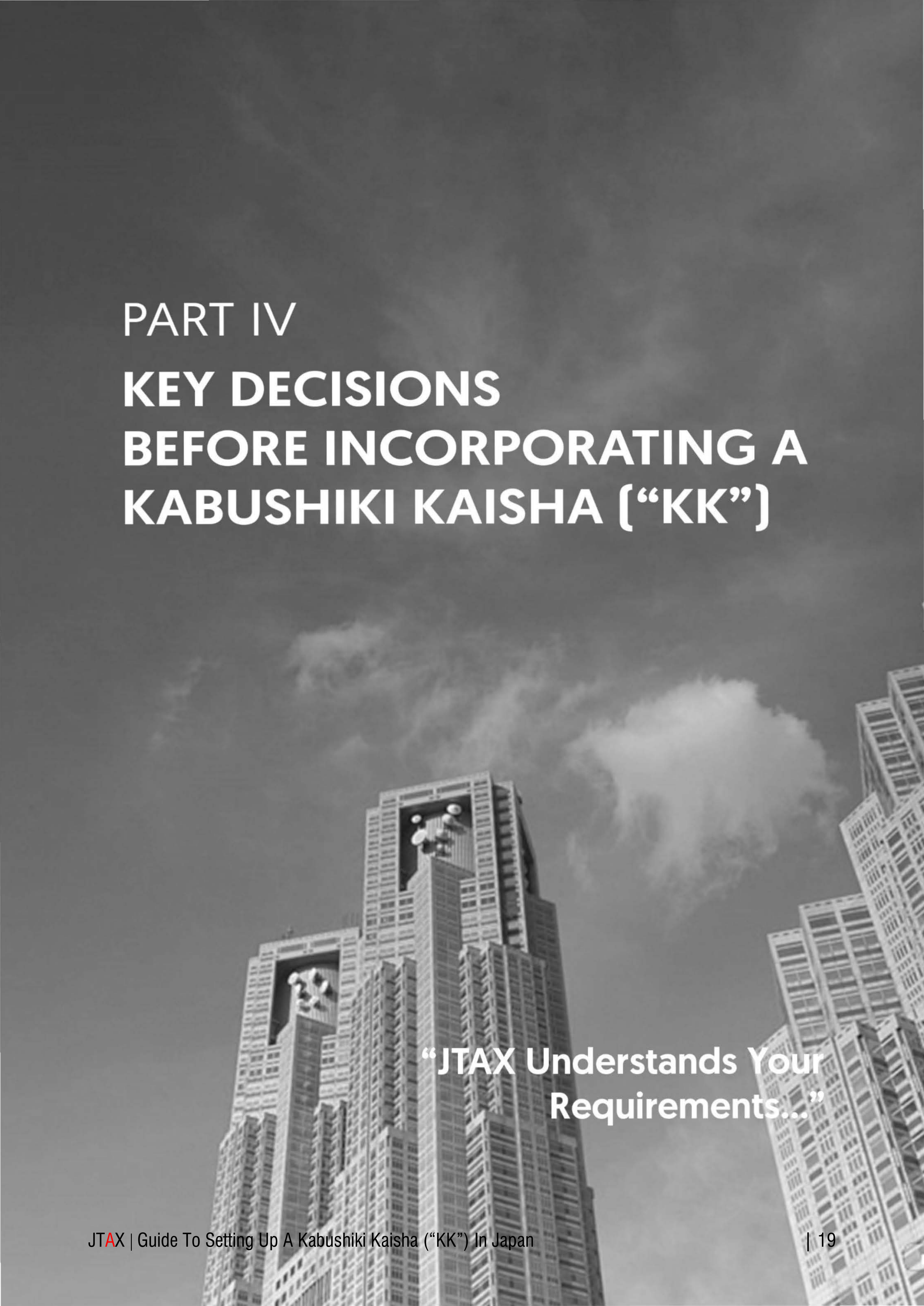
6. Audit Requirements

There is no general requirement that a Kabushiki Kaisha ("KK") be subject to an annual Commercial Code audit by an external Certified Public Accountant ("CPA").

However, an external Commercial Code audit is required for Kabushiki Kaisha ("KK") with paid in capital in excess of JPY500m, Kabushiki Kaisha ("KK") with liabilities of over JPY2 billion and / or those Kabushiki Kaisha ("KK") that have publicly traded securities.

PART IV

KEY DECISIONS BEFORE INCORPORATING A KABUSHIKI KAISHA ("KK")



"JTAX Understands Your Requirements..."

There are four important issues that need to be decided prior to a Kabushiki Kaisha ("KK") incorporation moving forward:

1. Directors

A Kabushiki Kaisha ("KK") requires at least one director and at least one individual must be nominated as the Representative Director.

A director must be a natural person (i.e., not a corporate entity).

From 1 April 2015, the requirements were simplified such that the requirement for a Japan resident director has been removed and a single director Kabushiki Kaisha ("KK") is now possible.

That said, most foreign investors will still appoint a Japan resident director for a Kabushiki Kaisha ("KK"). Having a Japan resident director will facilitate the establishment of a Japan bank account and also make it easier to enter agreements such as office leases.

<u>A decision to have no Japan resident director should be carefully considered since it may render business difficult (if not impossible).</u>

It should be noted that there are adverse individual and / or corporate tax consequences associated with an individual acting as a director of a Japanese company.

JTAX may be able to provide a qualified individual to fill the Kabushiki Kaisha ("KK") Japan resident director position via its **Japan Nominee Director Service.**

2. Shareholders

A Kabushiki Kaisha ("KK") needs at least one shareholder. The shareholder can be either an individual or an incorporated entity.

The residence of the shareholder can have important implications for such issues as withholding taxes on interest, dividends, and royalties paid from Japan.

3. Address in Japan

Three important issues need to be considered with respect to the Kabushiki Kaisha ("KK") address in Japan:

- **Legal registration issues**

A Kabushiki Kaisha ("KK") requires a legal registered address in Japan. Care should be taken in choosing this address since changes can be both costly (often several thousand USD) and time consuming (a month or more.)

- **Business address to receive phone calls, mail, etc.**

Separate to the legal registered address, a business address is often required. This function can be handled by the new Kabushiki Kaisha ("KK") "real" office. An alternative may be a virtual office service that is able to provide phone answering, mail collection, etc.

- **Visa issues**

Where visas for foreign employees may be required, a functioning business office will generally be needed. Virtual offices are usually not acceptable for visa purposes but a serviced office may be a workable solution.

JTAX is able to assist clients to meet their Japan office requirements in a cost effective manner. The premises used for our Japan Registered Address and Japan Virtual Office Services are located in a prime area of Tokyo and the office is owned by JTAX (thus ensuring long term stability.)

4. Paid in Capital

Paid in Capital represents the amount of cash (and sometimes other assets) that the owners contribute to a Kabushiki Kaisha ("KK") as equity.

Paid in capital can be used as working capital in the business after the incorporation has been completed.

In addition to working capital requirements, there are four additional issues that are relevant when considering paid in capital:

- ## Japanese VAT (Japanese Consumption Tax)

New Kabushiki Kaisha ("KK") with JPY10 million or more in paid in capital are generally automatically required to file a Japanese consumption tax (VAT) return.

Paid in capital of less than JPY10 million may give rise to Japanese consumption tax planning opportunities.

- ## Commercial image

The amount of paid in capital is available in the public record. Japanese customers and potential business partners may be reluctant to do business with a Japan entity that has low paid in capital. In addition, low paid in capital may cause difficulties when negotiating with landlords to enter an office lease.

- ## Tax based on paid in capital

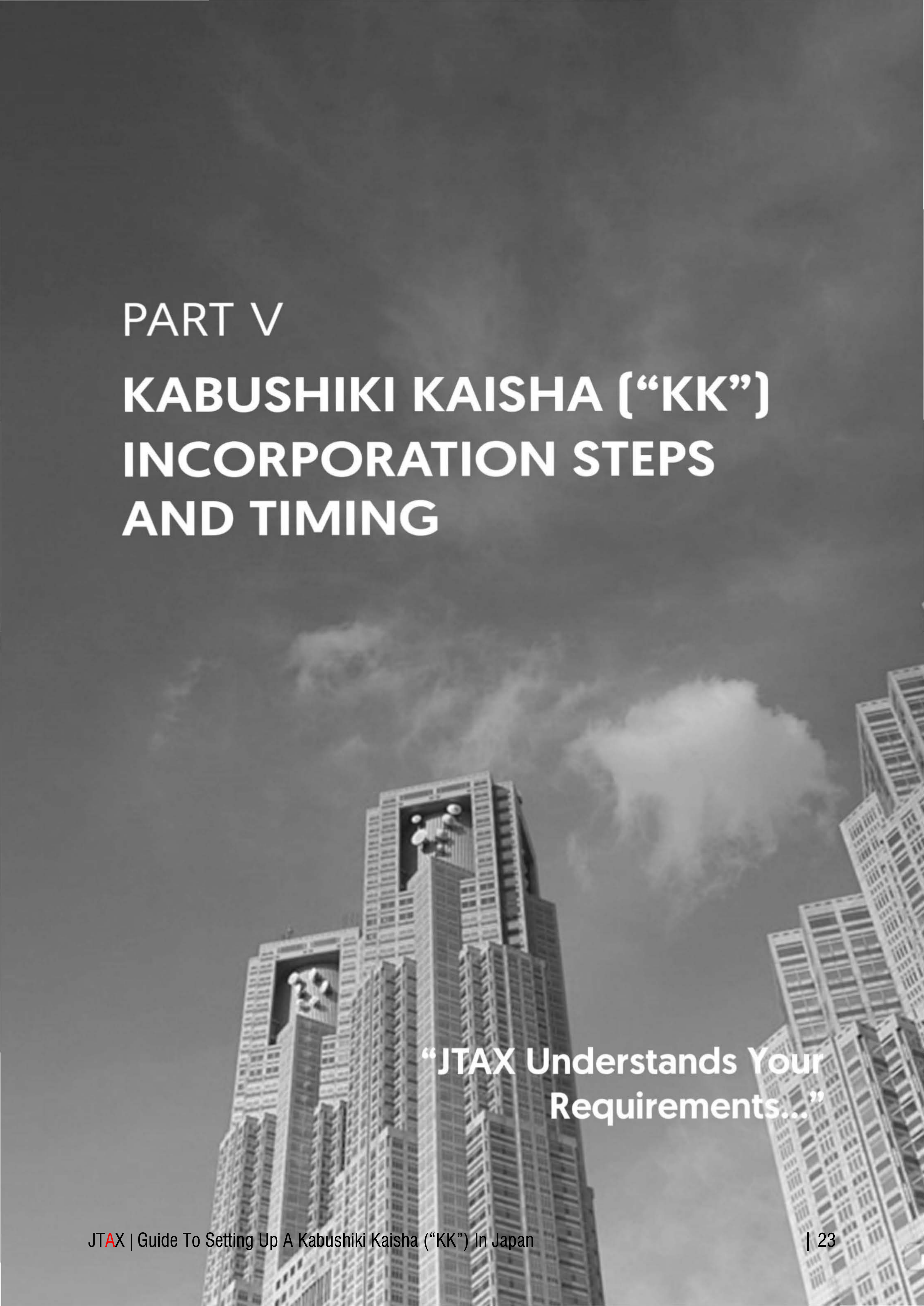
One component (though typically small) of calculating a Kabushiki Kaisha ("KK") tax liability is the level of paid in capital.

- ## Visa issues

Where there are plans that the Kabushiki Kaisha ("KK") will sponsor Japan work visas for foreign employees, the paid in capital must be high enough to demonstrate that the Japan operation is a viable business.

The following table provides additional guidance that may help you choose a level of paid in capital that best matches your requirements.

Amount of Paid in Capital	Comment
JPY1	Technically permissible but likely to create a poor commercial image. In particular, it may be difficult to lease an office and it may be difficult to find potential business partners.
JPY1 million	Often a reasonable compromise for companies that do not wish to contribute a high amount of paid in capital.
JPY5 million	Considered the lowest acceptable amount if the company will need to sponsor Japan work visas.
JPY10 million	This is the traditional minimum amount and is likely to be viewed favorably by potential business partners in Japan.



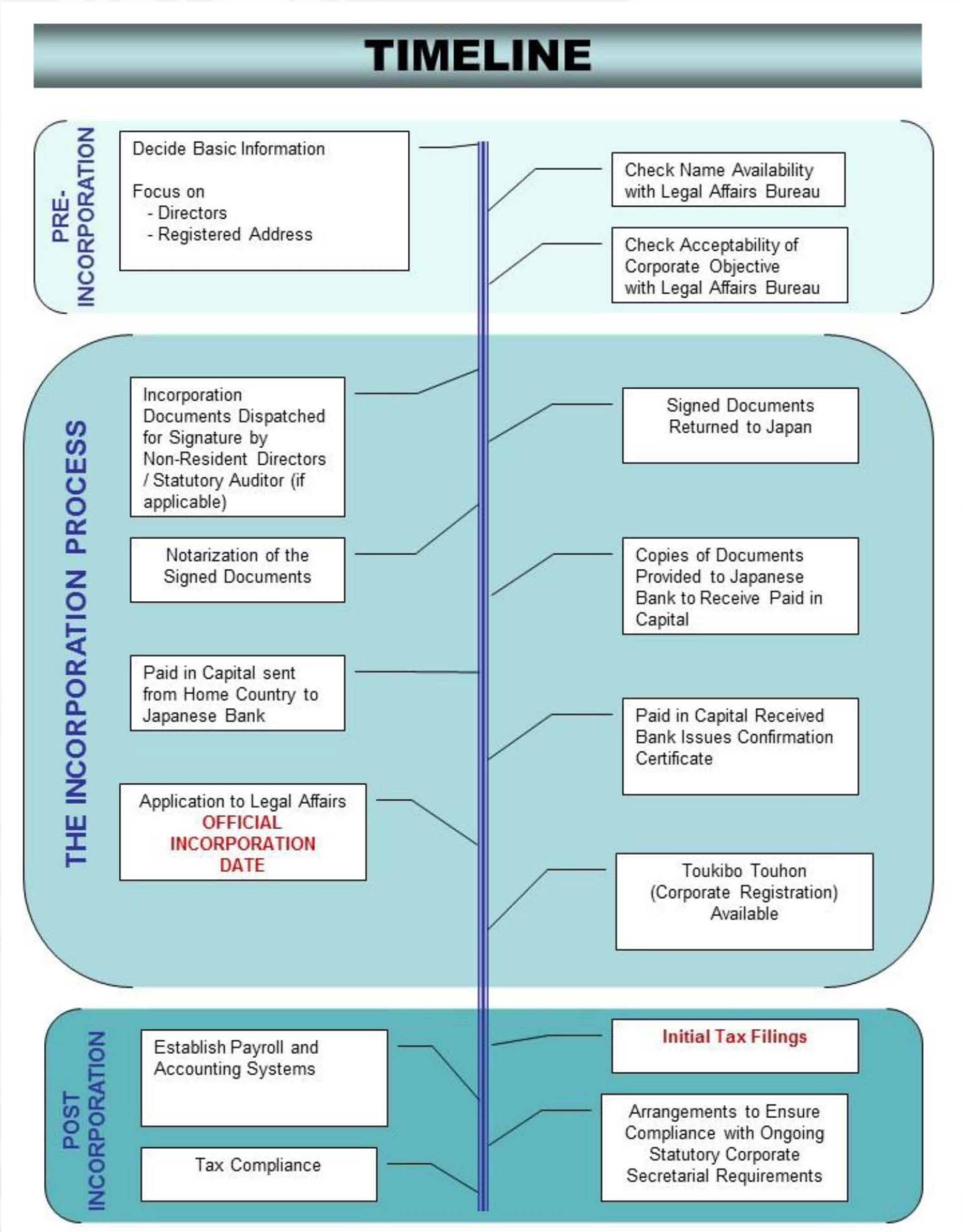
PART V

KABUSHIKI KAISHA (“KK”) INCORPORATION STEPS AND TIMING

“JTAX Understands Your Requirements...”

1. Overview of Steps to Incorporate A Kabushiki Kaisha ("KK")

The following graphic provides a simplified overview of the practical steps involved in incorporating a Kabushiki Kaisha ("KK") in Japan.



2. Time To Incorporate

Although a faster incorporation may be possible in an emergency, a Kabushiki Kaisha ("KK") incorporation generally takes between four and six weeks.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To learn more about how JTAX can help your company succeed in Japan, please contact one of our Japan-based professionals.
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