22 November 2019

Indirect Tax Alert

Japan: Overview of consumption tax hike and related tax reforms

Executive summary

The Japanese consumption tax increased to 10% on 1 October 2019 alongside the introduction of a new reduced rate system. The consumption tax in Japan now consists of two different rates: the standard rate of 10% and a reduced rate of 8%. This change will be followed by the introduction of the Qualified Invoice System (commonly referred to as the Japan Invoice Method) as the primary requirement for crediting input consumption tax from 1 October 2023 onward. The Itemized Invoice System will be adopted as a transitional measure prior to the introduction of the Qualified Invoice System. The timeline for reforms relating to these invoice systems is outlined below.

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Timeline for reforms relating to invoice systems
1 October 2019 Consumption tax rate increases to 10% ▸ *Introduction of reduced rate* ▸ *Introduction of the Itemized Invoice System*
31 March 2021 Special measure requiring the display of tax-inclusive amounts expires
1 October 2021 Registration of Qualified Invoice issuers begins
1 October 2023 ▸ *Introduction of the Qualified Invoice System*

Detailed discussion

Consumption tax hike

The consumption tax rate increased to 10% on 1 October 2019 alongside the simultaneous introduction of a reduced rate of 8%. Taxable transactions taking place on or after 1 October 2019 are subject to either the standard rate of 10% or the reduced rate of 8%.

	Until 30 September 2019 (Single tax rate)	From 1 October 2019 (Multiple tax rates)	
		Standard rate	Reduced rate
(National) consumption tax rate	6.3%	7.8%	6.24%
Local consumption tax rate	1.7%	2.2%	1.76%
Overall consumption tax rate	8.0%	10.0%	8.0%

Transitional measures

In the same manner as the transitional measures introduced with the previous tax hike from 5% to 8%, certain transactions taking place on or after 1 October 2019 are subject to transitional measures which provide for the application of the former rate of 8%. However, the transitional measures do not apply to transactions subject to the reduced rate. A summary of the transitional measures is as follows:

- Transitional measures (with a reference date of 1 April 2019)
  - Contract construction work: Taxable transactions taking place on or after 1 October 2019 in accordance with a construction work-related contract concluded between 1 October 2013 and 31 March 2019.
  - Lease of assets: The lease of assets on or after 1 October 2019 conducted in accordance with a contract concluded between 1 October 2013 and 31 March 2019, provided that the lease began prior to 1 October 2019.
  - Mail orders: The distribution of products on or after 1 October 2019 in accordance with the sales price and other terms offered before (or for which the preparation to conduct such offers was completed prior to) 1 April 2019 by a mail-order business and concerning which orders were received prior to 1 October 2019. Transactions subject to the reduced rate are excluded from this transitional measure.

- Transitional measures (with a reference date of 1 October 2019)
  - Passenger fares: Passenger fares and fees for admission to movie and performing theaters, horse racing venues, track cycling venues, art museums and amusement parks, among others, which were paid prior to 1 October 2019.
  - Electricity charges: Charges for electricity, gas, water, telecommunications or kerosene supplied continuously since a date prior to 1 October 2019 and for which the right to receive the payment of such charges is established between 1 October 2019 and 31 October 2019, in accordance with contracts for the continuous supply of said utilities.

Implementation of the reduced rate system

The following transactions (sales) taking place on or after 1 October 2019 are subject to a reduced rate of 8%, comprised of a national tax of 6.24% and a local tax of 1.76%.

- Food and drink (excluding liquor, takeout food and catering); Food and drink withdrawn from bonded areas are also subject to the reduced rate
- Newspapers issued at least twice a week in accordance with a subscription contract

Requirements on accounting records and invoices

As the consumption tax now consists of two different rates, accounting records must state which taxable purchases are subject to the reduced rate in order to credit input consumption tax paid for taxable purchases. Moreover, under the Itemized Invoice System, invoices must state which items are subject to the reduced rate, have subtotal tax-inclusive amounts aggregated by tax rate, and be stored along with other relevant documents.

Qualified Invoice System

The Itemized Invoice System described above will be replaced by the Qualified Invoice System (commonly referred to as the Japan Invoice Method) on 1 October 2023. Under the Qualified Invoice System, the principle requirement for the crediting of input consumption tax will be the storage of qualified invoices which contain certain types of information including registration numbers and applicable tax rates. Qualified invoices will be issued by businesses which submit applications to a tax office and are registered as Qualified Invoice Issuers. Note that only taxable businesses can be registered as Qualified Invoice Issuers.

In principle, input consumption tax paid for taxable purchases from businesses other than Qualified Invoice Issuers, such as consumers and tax-exempt businesses, is not creditable. Notwithstanding the above, a transitional measure will allow for a certain ratio of input consumption tax to be credited and will be applicable for the designated periods described below.

Period	Creditable ratio
1 October 2023 to 30 September 2026	80% of input consumption tax
1 October 2026 to 30 September 2029	50% of input consumption tax

For additional information with respect to this Alert, please contact the following:

Ernst & Young Tax Co., Chiyoda-ku

- Yoichi Ohira yoichi.ohira@jp.ey.com
- Nami Okuyama nami.okuyama@jp.ey.com

Ernst & Young LLP (United States), Japan Tax Desk, New York

- Hiroaki Ito hiroaki.ito1@ey.com

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