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Japan Tax Bulletin

Taxation of 100%-ownership domestic group

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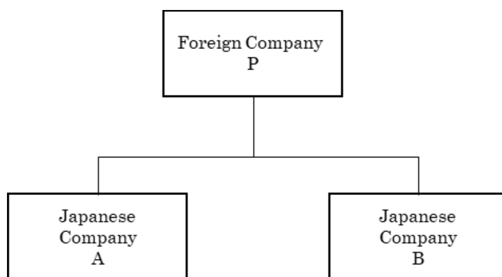
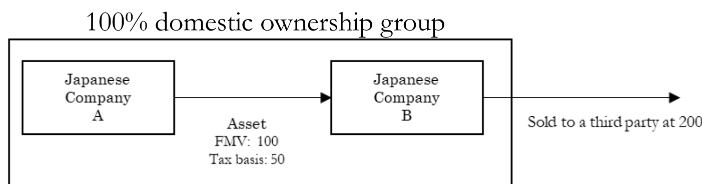
There are special taxation rules for transactions between companies in a 100%-ownership domestic group. This bulletin summarizes these rules as below:

1. *100%-ownership domestic group*

A 100% ownership domestic group is a group of domestic companies where one company wholly owns another company directly or indirectly, or both companies are wholly owned by the same person. Where the same person is an individual, individuals who have special relationships, such as family members, are counted as the same person. JCo A and JCo B in the chart below are in a 100%-ownership domestic group.



2. *Deferral of gains or losses for transactions between companies in a 100%-ownership domestic group*



Where JCo A sells an asset at 100 with tax basis 50 to JCo B, recognition of the gain amounting to 50 by JCo A is deferred until the asset leaves the group i.e. until JCo B sells it to a third party or it is otherwise disposed of.
The following assets qualify under the deferral rule:

- Fixed assets
- Land owned as inventory
- Securities (securities held for trading purposes by a transferor company or a transferee company are excluded)
- Monetary claims
- Deferred assets

3. *Intercompany dividends*

Where a Japanese company receives a dividend from wholly owned domestic subsidiary, the dividend received is excluded from taxable income entirely.

The exclusion of a domestic intercompany dividend is reduced to 50% where more than 5% to 1/3 ownership and 20% where 5% or more ownership.

4. *Economic gains*

Where companies are in a 100%-ownership domestic group where individuals are not involved, economic gains one company received from the other company are not included in taxable income as long as the other company treats the transfer the economic gains as donation expenses, which are subject to a limitation on deductibility.

The following example illustrates the treatment.

Company A and Company B are in a 100%-ownership domestic group. Company A sold an asset with a fair value and tax basis of 100 and 50 respectively for 70 in cash. The economic gain recognized by Company B is not included in its taxable income and the donation expense of Company A is subject to the deduction limitation

The tax journal entries for Company A are as follows:

Cr		Dr	
Cash	70	Revenue	100
Donation expense	30		
Cost	50	Asset	50

The tax journal entries of Company B are as follows:

Cr		Dr	
Asset	100	Cash	70
		Economic gain	30

Where Company A and Company B is not in a 100%-ownership domestic group, the economic gain recognized Company B would be included in its taxable inc

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