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Japan Tax Bulletin

Depreciation under Japan corporate tax law

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The calculation method for depreciation under Japan corporate tax law is one of the most complicated tax issues to understand. This bulletin provides an overview of the tax rules relating to depreciation as discussed below:

1. Basic rules for the deductibility of depreciation

Under corporate tax law, the deductibility of depreciation is based on the amount that a company books during its financial year, up to a limit which is calculated using a certain method for each category for tax purposes.

2. Acquisition cost

The acquisition cost of depreciable assets includes the initial purchase price and additional costs of obtaining the assets to put to use in a business.

3. Calculation of ordinary depreciation

3.1 Categories of assets

Depreciable assets are categorized as follows:

(i) Tangible assets

- buildings and facilities
- structures
- machinery and equipment
- ships, aircraft and vehicles
- tools, appliances and fixtures
- certain animals and fruit trees

(ii) Intangible assets

- software
- goodwill
- patents and trademarks
- utility model rights, design rights
- other rights for mining, fishing, water use, railway, electricity or gas etc.

3.2 Useful lives of assets

The useful lives of depreciable assets are stipulated in the ordinance of the Ministry of Finance.

3.3 Allowable methods of depreciation

Statutory depreciation methods are set in each asset category, and companies may apply for permission from the tax office to use different depreciation methods in certain categories.
Only the straight-line method is allowed for buildings (acquired after 1 April 1998) and facilities (acquired after 1 April 2016), structures (same as facilities) and intangible assets generally.
Allowable depreciation methods are as follows:

(i) Straight-line method

A method calculated by multiplying the acquisition cost of the depreciable asset by the depreciation rate corresponding to the useful life of the asset. This gives the depreciation limit for each financial year, so that the depreciation expense is the same in each financial year.

(ii) Reducing balance method

A method calculated by multiplying the net book value (NBV) for tax purposes of the depreciable asset by the depreciation rate corresponding to the useful life of the asset. This gives a depreciation limit that reduces in each financial year.
The "NBV for tax purposes" means the amount after deducting the total depreciation for tax purposes charged in previous years from the acquisition cost of the asset.

3.4 Calculation of tax adjustment

If the amount of depreciation booked exceeds the limit calculated by the methods above, the excess amount is deemed to not be claimed.
The excess amount is considered on an item by item basis.
If the amount of depreciation booked is less than the limit, the booked amount is deducted for tax purposes.

For example:

a. Book amount > Limit

Book depreciation	JPY 100
Limit	JPY 50
Deduction allowed	JPY 50

b. Book amount ≦ Limit

Book depreciation	JPY 100
Limit	JPY 150
Deduction allowed	JPY 100

Where the corporate depreciation policy for financial reporting purposes is different from the depreciation rules for tax purposes, tax adjustments are made on tax return.

3.5 Carry forward

If the company has an asset where the booked depreciation exceeded the limit in prior financial years, the excess amount is carried forward to the following financial years.
The excess amount will be deducted in a financial year when the depreciation is less than the limit amount, as an additional deduction up to the limit.

For example:

Excess amount carried forward	JPY 50
Book depreciation	JPY 100
Limit	JPY 120
Deduction allowed	JPY 100 + 20
Excess amount carried forward to following year	JPY 30

4. Treatment for asset disposals

When a company disposes of an asset, the remaining NBV and carried forward tax adjustment amount are deducted in the financial year of disposal for tax purposes.

5. Depreciation allowance for short term assets and small items

If a company acquires a depreciable asset which is expected to last for less than one year or costing is less than JPY 100,000 and the company books its acquisition cost as an expense in the acquired financial year, the expensed amount is deductible for tax purposes.

6. Calculation of lump-sum depreciation

If a company acquires assets (excluding leased assets and assets described in section 5) costing less than JPY 200,000 the company can choose the "Lump-sum" method as the depreciation method for these assets.

Under the Lump-sum method, the acquisition cost of assets are grouped by financial year, and the depreciation limit is calculated on a straight-line basis with the useful life as three years. The way of calculating the tax adjustment is the same as for ordinary assets.

Even if one of the lump-sum assets is disposed of within three years, the company is required to continue the calculation with the lump-sum method over the useful life.

7. Special treatment for SMEs[1]

For an SME (except SMEs whose average profit for last three financial years is over JPY 150 million), assets costing less than JPY 300,000 and booked as an expense, are entirely deductible when acquired with a cap of JPY 3 million.

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1 An SME is a corporation whose stated capital is JPY 100 million or less. Even where the stated capital is JPY 100 million or less, a corporation does not qualify as an SME if 100% owned directly or indirectly by a corporation/corporations of whose stated capital is JPY 500 million or more (" Large corporation").

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