

Japan Inbound Tax & Legal Newsletter

Opportunities offered under the Connected Industries tax system

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In Brief

Introduced as part of the 2018 tax reform under the Act on Special Measures for Productivity Improvement, the Connected Industries tax system (IoT tax system) provides preferential tax measures to support certain capital investment (i.e. the introduction of systems, sensors, etc.) that boost productivity through collaboration and utilization of data. Companies using equipment, software, machinery or other devices with functions within the scope of the IoT tax system may be entitled to certain tax benefits in the year the assets are acquired, including additional depreciation of 30% on the relevant assets or a tax credit of 3% of the cost of the equipment against their corporate tax liability (increased to 5% in certain instances), assuming the required conditions are met.

This alert outlines the operation of the relief and highlights the types of company that have been successful in applying for IoT tax system incentives. Taxpayers' plans must be submitted and approved, and the assets acquired, prior to 31 March 2021.

1. Overview of the IoT tax system

The IoT tax system was introduced as from 6 June 2018 to increase business productivity by promoting the development and use of information technology (e.g. the internet of things and artificial intelligence) and data analytics. The incentives available under the system are not limited to entities registered in Japan, and eligible Japanese branches of foreign corporations also may apply. To be eligible, companies must meet all of the following requirements:

1. File a blue form tax return

A taxpayer who does not already have blue form tax return status must submit an application for such status by the beginning of the relevant year, or for newly-formed companies, by the end of the first fiscal year. Taxpayers with blue form status are afforded certain benefits (e.g. the ability to carry forward losses, eligibility for special tax incentives, etc.) and must meet specific requirements in relation to their accounting systems and record-keeping.

2. Submit plan and receive certification for use of innovative data

Companies must submit a plan to the Ministry of Economy, Trade, and Industry prior to 31 March 2021. The plan must contain specific information, including details of the purpose of using/sharing data via information technology, cybersecurity measures, descriptions of the expected enhancements in labor productivity and return on investment, and information regarding the assets to be used. An expected increase of at least 2% in labor productivity and a 15% return on investment are required. The plan's cybersecurity measures must be certified by a Registered Information Security Specialist prior to submission. Once submitted, plans must be certified by the relevant minister before acquisition of the equipment.

3. Acquire equipment that uses the information sharing technology described in the company's certified plan

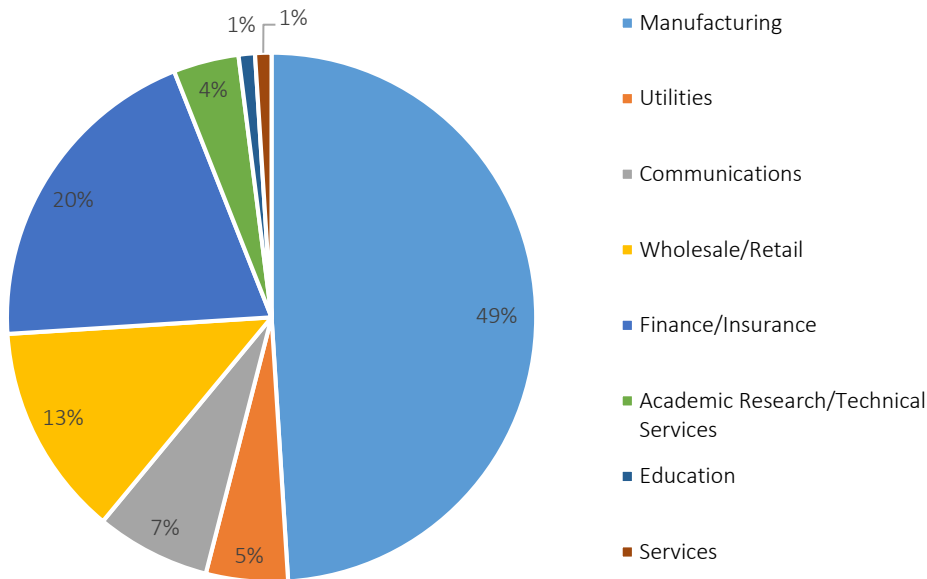
Eligible equipment under the IoT tax system includes software, devices, etc. with an acquisition cost of at least JPY 50 million that utilizes the information sharing capabilities. To obtain certification, the equipment must be acquired in the period from 6 June 2018 to 31 March 2021. Assets to be used for leasing or R&D activities are not eligible.

Companies that successfully apply for the IoT tax system are entitled to enhanced depreciation of 30% on the applicable assets or a tax credit of 3% (limited to 15% of the corporate tax payable). Companies whose employees have received at least a 3% increase in their pay/allowances compared to the previous year are entitled to an increased credit of 5% (limited to 20% of the corporate tax payable).

2. Companies utilizing the IoT tax system

Although generally viewed as a benefit geared toward manufacturing companies, the IoT tax system is not limited to manufacturing and is available to companies in various industries and sectors (with certain exceptions such as software, data processing, etc.). As of 31 July 2019, 85 companies had successfully applied for the incentive. Approximately 88% of these are large companies with stated capital in excess of JPY 100 million and around 49% are manufacturing companies. Companies in various other industries and sectors also have been successful, as depicted below:

IoT tax system companies by industry



Source: [HP of Ministry of Economy, Trade and Industry](#)

Deloitte's view

The IoT tax system can provide additional tax incentives for companies intending to adopt information technology that meets the necessary criteria. Japanese companies and foreign companies with Japanese branches in all industry sectors should be aware of the system and consider whether they may be eligible to benefit from the available incentives. Companies may wish to consult with their tax advisors and IT specialists to explore whether the system can be used effectively before it expires on 31 March 2021. The approval process takes at least one month (potentially longer depending on the circumstances) and companies should ensure that they apply with sufficient lead time to enable implementation before the eligibility period expires.

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