

Companies Seek Reforms to the Corporate Tax System —Nissay Business Conditions Survey (August 2003)

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1. Introduction

The corporate tax system is an important determinant of corporate behavior. With recent signs of a budding economic recovery, there have been growing calls to reduce the corporate income tax rate and help the recovery generate momentum. In addition, some have argued that Japan needs to cut its corporate income tax rate to the level of other countries so as to boost international competitiveness. Meanwhile, other changes are occurring in the tax system, including new deductions introduced this fiscal year for R&D and capital investment spending, and a pro forma standard tax slated for introduction in the local corporate income tax next year.

Given the ongoing changes in the economy and corporate tax system, the latest Nissay Business Conditions Survey (conducted in August 2003 jointly by Nippon Life Insurance Co. and NLI Research Institute, with valid responses from 2,308 companies nationwide) takes a closer look at the opinions of companies toward corporate tax reform.

According to survey results, 55% of companies are dissatisfied with the present corporate tax system, and over 70% call for a reduction in the corporate income tax rate. In response to this fiscal year's new tax deductions to encourage spending on R&D and capital investment, only about 20% of companies have or will increase spending; and approximately 40% want the pro forma standard tax either reduced or abolished.

2. On the Present Corporate Tax System

With regard to the present corporate tax system, only 0.1% of companies are "satisfied" and another 2.9% are "fairly satisfied" (Figure 1). On the other hand, over half (55.3%) of companies express at least some dissatisfaction: 11.4% are "dissatisfied," and another 43.9% are "somewhat dissatisfied."

By industry sector, companies in process manufacturing tend to be slightly more satisfied (or fairly satisfied) than in materials manufacturing and non-manufacturing. By company size, a

higher proportion of second-tier companies and small & medium companies are dissatisfied (12.9% and 11.2% respectively) than large companies, indicating that smaller companies tend to be more dissatisfied with the corporate tax system. By business conditions, more companies experiencing bad or somewhat bad conditions are dissatisfied (13.6%) or somewhat dissatisfied (45.0%) than companies with normal or good conditions.

Figure 1 Opinion of the Present Corporate Tax System

	Satisfied	Fairly satisfied	Can't say	Somewhat dissatisfied	Dissatisfied
All industries	0.1	2.9	40.4	43.9	11.4
Sector					
Materials manufacturing	0.0	2.8	39.0	43.6	12.8
Process manufacturing	0.2	4.4	40.5	44.2	9.6
Non-manufacturing	0.1	1.8	40.1	44.5	12.4
Company size					
Large	0.0	1.6	40.8	46.1	7.9
2nd-tier	0.1	2.9	37.9	45.5	12.9
Small & medium	0.1	2.9	41.6	43.0	11.2
Business conditions					
Good, somewhat good	0.0	2.7	41.8	42.5	11.5
Normal	0.1	2.9	43.7	43.4	8.5
Bad, somewhat bad	0.1	2.8	37.7	45.0	13.6

Note: Numbers may not add up to 100 due to incomplete responses.

As for why they are dissatisfied, companies overwhelmingly cite the high corporate tax rate (62.2%), followed by the complicated procedures for receiving tax deductions (40.6%), and planned introduction of the pro forma standard tax (24.0%).

By sector, process manufacturing tends to emphasize the high tax rate (65.4%) and inadequacy of the new tax deductions (19.0%), while materials manufacturing emphasizes inadequacy of the consolidated tax system (13.6%), and non-manufacturing emphasizes the complicated tax payment (42.3%). By company size, a high proportion of large companies cite introduction of the pro forma standard tax (35.9%) and inadequacy of the consolidated tax system (24.3%). Companies reporting good business conditions tend to emphasize the high tax rate (67.2%) and inadequacy of tax deductions for R&D and capital investment spending (18.4%).

Figure 2 Reasons for Dissatisfaction with Current Tax System

(%)

	Tax rate too high	New tax deductions are inadequate	Lacks consideration for small & med. cos.	Consolidated tax system is inadequate	Oppose pro forma standard tax	Tax procedures too complex	Other
All industries	62.2	13.8	21.8	11.0	24.0	40.6	6.1
Sector							
Materials manufacturing	61.6	14.6	18.7	13.6	22.2	38.9	6.6
Process manufacturing	65.4	19.0	17.6	9.2	22.6	38.0	7.5
Non-manufacturing	61.5	10.8	25.1	10.6	24.9	42.3	5.0
Company size							
Large	47.6	13.6	5.8	24.3	35.9	39.8	10.7
2nd-tier	63.4	12.3	10.3	14.8	28.6	43.6	7.8
Small & medium	63.4	14.6	30.0	7.1	20.2	39.2	4.7
Business conditions							
Good, somewhat good	67.2	18.4	18.9	11.5	22.1	37.7	5.3
Normal	61.2	12.3	19.5	13.1	23.0	39.3	6.7
Bad, somewhat bad	60.7	13.0	24.6	9.5	25.3	42.7	4.1

Notes: For companies who responded they are "dissatisfied" or "somewhat dissatisfied" to the present corporate tax system. Numbers may not add up to 100 due to multiple response (up to two responses).

3. 70% Want Corporate Income Tax Rate Cut

Regarding the corporate income tax rate, over 70% of companies say the current tax rate is high: 23.0% call for an immediate tax rate cut, and another 49.9% for a tax rate cut in the future (Figure 3).

By sector, compared to process manufacturing, materials manufacturing and non-manufacturing sense a stronger need for an immediate tax rate cut (23.4% and 24.5% respectively). By company size, large companies tend to be more content with the present tax rate (25.7%), and less inclined toward a tax rate cut than second-tier and small & medium companies. No significant patterns are observed based on business conditions; overall, there is a strong call for a tax rate cut.

As for why a tax rate cut is needed, over 80% of companies cite economic vitalization, indicating that they believe a tax rate cut will stimulate corporate activity (Figure 4). This is followed by "to boost international competitiveness" (32.4%) and "because the corporate income tax burden exceeds that of other countries" (27.1%).

By sector, boosting international competitiveness is emphasized in the manufacturing sector, which faces intense foreign competition. In addition, Japan's high corporate tax burden compared to other countries is also stressed in materials manufacturing. On the other hand, a high proportion of non-manufacturing companies cites economic vitalization (86.5%). By

company size, emphasis on boosting international competitiveness tends to increase with company size, while loss of entrepreneurial spirit decreases. By business conditions, emphasis on boosting international competitiveness increases as business conditions improve.

Figure 3 Opinion on the Present Corporate Tax Rate

(%)

	Rate cut needed now	Rate cut needed later	No change needed	Rate hike needed	Other
All industries	23.0	49.9	20.4	2.6	2.1
Sector					
Materials manufacturing	23.4	50.7	20.5	2.3	1.4
Process manufacturing	20.8	53.4	19.1	3.0	2.6
Non-manufacturing	24.5	48.3	20.6	2.4	2.2
Company size					
Large	17.3	48.2	25.7	2.1	2.6
2nd-tier	23.9	51.2	18.9	2.9	1.6
Small & medium	23.3	49.7	20.4	2.6	2.3
Business conditions					
Good, somewhat good	23.5	50.2	18.4	3.5	2.0
Normal	19.1	52.4	21.8	2.6	2.3
Bad, somewhat bad	25.5	48.4	20.2	2.4	2.1

Note: Numbers may not add up to 100 due to incomplete responses.

Figure 4 Why the Corporate Tax Rate Must be Reduced

(%)

	To vitalize economy	To boost intl. competitiveness	Corporate tax burden exceeds other countries	Stifles entrepreneurship	Should expand pro forma tax instead	Other
All industries	80.9	32.4	27.1	18.1	4.4	2.2
Sector						
Materials manufacturing	73.1	42.7	30.8	18.1	2.7	0.8
Process manufacturing	76.5	43.0	23.9	17.8	5.7	2.2
Non-manufacturing	86.5	22.6	27.1	19.1	4.3	2.8
Company size						
Large	76.8	43.2	25.6	9.6	3.2	2.4
2nd-tier	82.7	38.0	27.7	13.3	4.7	1.9
Small & medium	80.6	28.4	26.8	21.6	4.4	2.3
Business conditions						
Good, somewhat good	78.7	39.6	24.3	21.3	5.4	1.2
Normal	80.3	33.7	28.5	16.1	4.5	2.3
Bad, somewhat bad	82.3	28.3	27.4	18.3	3.8	2.5

Notes: For companies who responded "rate cut needed now" and "rate cut needed later." Numbers may not add up to 100 due to multiple response (up to two responses).

4. Only 20% Respond to New Tax Deductions

Regarding whether the tax deductions introduced this fiscal year for R&D and capital investment spending will cause companies to increase spending, 52.7% say no. Only about 20% responded affirmatively: 5.0% have increased spending or will do so, and 14.6% are considering doing so (Figure 5).

Figure 5 Effect of Tax Deductions on R&D and Capital Investment Spending (%)

	Increased spending (or will)	Considering an increase	Will not increase spending	Unaware of tax cut	Other
All industries	5.0	14.6	52.7	5.2	15.9
Sector					
Materials manufacturing	7.1	18.8	56.1	2.6	10.3
Process manufacturing	6.2	20.2	56.5	3.3	10.5
Non-manufacturing	3.9	10.0	50.3	7.1	20.4
Company size					
Large	4.2	19.9	50.8	4.2	10.5
2nd-tier	5.3	14.6	56.8	3.4	14.5
Small & medium	5.0	13.8	51.3	6.2	17.4
Business conditions					
Good, somewhat good	8.4	21.2	41.8	7.3	15.7
Normal	5.0	13.8	53.4	2.4	17.2
Bad, somewhat bad	3.6	12.3	57.0	6.5	15.3
On the income tax rate					
Rate cut needed now	6.6	16.9	47.3	6.2	16.4
Rate cut needed later	5.2	16.2	53.1	4.8	16.0
No change needed	3.4	10.0	61.3	5.5	14.9
Rate hike needed	3.3	14.8	59.0	4.9	13.1

Note: Numbers may not add up to 100 due to incomplete responses.

By sector, manufacturing is more inclined to consider or actually increase spending than non-manufacturing. However, companies are not always well informed about tax cuts; among non-manufacturing companies, 7.1% were not even aware of the preferential tax measures. The proportion of companies considering or actually increasing spending tends to increase with company size and favorable business performance. The inclination to spend also tends to increase among companies who strongly favor a corporate tax rate cut.

As to why companies do not increase spending on R&D and capital investment, the overwhelming reason is that they have no pressing need to do so (64.4%; Figure 6).

By sector, the lack of spending needs is most commonly cited in non-manufacturing (72.3%), while the inadequacy of tax deductions and special depreciation measures is most common in

process manufacturing (9.3%). Loss-making performance as a reason is prominent in materials manufacturing (10.2%). By company size, the lack of spending needs is cited more often as size decreases (67.2%). By business conditions, companies reporting good conditions tend to emphasize the inadequacy of deductions and special depreciation measures (8.5%).

Figure 6 Reasons Not to Boost R&D or Capital Spending (%)

	No need	Tax measures are inadequate	Loss-making company	Other
All industries	64.4	6.2	6.9	20.5
Sector				
Materials manufacturing	66.0	4.1	10.2	18.8
Process manufacturing	53.2	9.3	7.2	27.7
Non-manufacturing	72.3	5.3	5.3	15.7
Company size				
Large	51.5	4.1	8.2	33.0
2nd-tier	62.4	6.7	5.2	24.2
Small & medium	67.2	6.2	7.7	16.8
Business conditions				
Good, somewhat good	61.9	8.5	3.7	23.3
Normal	66.4	5.3	4.1	22.3
Bad, somewhat bad	64.1	6.0	9.9	18.0

Notes: For companies who responded "will not increase spending." Numbers may not add up to 100 due to incomplete responses.

5. On the Introduction of the Pro Forma Standard Tax

The pro forma standard tax, to be introduced in fiscal 2004 for corporations with at least ¥100 million in paid-in capital, will replace part of the local corporate income tax with a formula based on value added and paid-in capital. In our survey, 28.7% of companies oppose its introduction, while 19.6% have no objections in particular. And while 12.5% want the scope of companies and tax amount reduced, another 12.0% want the scope of companies and tax amount expanded. Thus overall, 41.2% want the pro forma tax reduced or abolished (Figure 7).

By sector, other than that non-manufacturing companies are less affected by the tax, no significant tendencies are observed. By business conditions, companies with bad conditions are more likely to oppose the tax or want the scope of companies and tax amount reduced, and less likely to have no objections to the tax. However, a high percentage of companies with bad business conditions (12.4%) also want the tax expanded. Also, opposition to the tax and calls for the reduction of its scope and amount increase as the level of dissatisfaction increases with the present tax system.

Figure 7 Opinion Regarding the Pro Forma Standard Tax

(%)

	Should expand scope & amount	Have no objections	Should reduce scope & amount	Opposed to tax	Other
All industries	12.0	19.6	12.5	28.7	22.8
Sector					
Materials manufacturing	13.4	20.5	14.5	29.9	16.2
Process manufacturing	12.2	21.8	12.5	28.6	21.7
Non-manufacturing	12.2	17.8	12.0	27.9	26.1
Business conditions					
Good, somewhat good	11.7	23.2	11.9	25.9	21.9
Normal	11.5	21.6	12.0	26.9	22.3
Bad, somewhat bad	12.4	16.5	13.1	31.3	23.9
Opinion of corporate tax system					
Satisfied (fairly satisfied)	22.1	22.1	10.3	7.4	33.8
Can't say	9.9	26.2	11.8	22.6	24.6
Dissatisfied (somewhat dissatisfied)	13.2	15.0	13.2	34.7	21.4

Note: Numbers may not add up to 100 due to incomplete responses.

Among companies favoring expansion of the pro forma tax in scope and amount, the most common reason is that “no corporation should be excluded from the tax” (45.3%), followed by “because the tax burden of loss-making corporations remains light” (34.5%), and “to stabilize fiscal revenue” (18.7%; Figure 8).

By sector, high responses are observed in process manufacturing for “no corporation should be excluded” (49.4%) and “the tax burden of loss-making corporations remains light” (39.5%). By company size, small and medium companies emphasize the light tax burden of loss-making corporations (35.7%), while second-tier companies emphasize “to stabilize fiscal revenue” (20.6%). No significant patterns are observed by business conditions.

Figure 8 Reasons to Expand Scope/Amount of Pro Forma Standard Tax (%)

	No corporation should be excluded from tax	Tax burden of loss-making corporations remains light	To stabilize fiscal revenue	Other
All industries	45.3	34.5	18.7	0.7
Sector				
Materials manufacturing	44.7	31.9	21.3	0.0
Process manufacturing	49.4	39.5	11.1	0.0
Non-manufacturing	43.4	33.1	21.4	1.4
Company size				
Large	46.2	34.6	15.4	0.0
2nd-tier	46.4	32.0	20.6	0.0
Small & medium	44.8	35.7	18.2	1.3
Business conditions				
Good, somewhat good	45.3	35.8	18.9	0.0
Normal	48.9	33.3	17.8	0.0
Bad, somewhat bad	43.2	34.1	19.7	1.5

Notes: For companies who responded "should expand scope & amount" of the pro forma standard tax. Numbers may not add up to 100 due to incomplete responses.

Among companies favoring reduction of the pro forma tax, the main reasons cited are that it "lacks consideration for second-tier companies" (28.5%), that they "object to the tax calculation method" (22.2%), and that it would "increase the tax burden significantly" (22.2%; Figure 9).

By sector, high responses are observed in materials manufacturing for "lacks consideration for second-tier companies" (31.4%) and "lacks consideration for loss-making corporations" (26.3%). On the other hand, process manufacturing emphasizes "object to the tax calculation method" (25.9%). By company size, the smaller the size, the greater the emphasis on "lacks consideration for second-tier companies" and "lacks consideration for loss-making companies," while the larger the size, the stronger the emphasis on "increases tax burden significantly." By business conditions, while companies experiencing bad conditions tend to emphasize "lacks consideration for loss-making companies," companies experiencing good conditions tend to emphasize "increases the tax burden significantly."

Figure 9 Reasons to Reduce or Abolish Scope/Amount of Pro Forma Standard Tax

(%)

	Lacks consideration for 2nd-tier companies	Lacks consideration for loss-making companies	Object to tax calculation method	Increases tax burden significantly	Other
All industries	28.5	20.3	22.2	22.2	3.5
Sector					
Materials manufacturing	31.4	26.3	17.3	21.8	2.6
Process manufacturing	29.3	22.0	18.7	22.7	2.6
Non-manufacturing	27.4	17.3	25.9	22.1	4.0
Company size					
Large	14.6	15.7	22.5	37.1	6.7
2nd-tier	23.6	17.4	27.0	24.8	3.4
Small & medium	33.7	22.9	19.2	18.2	3.0
Business conditions					
Good, somewhat good	27.5	12.9	22.2	28.1	3.5
Normal	28.3	17.4	22.4	25.0	4.3
Bad, somewhat bad	29.1	25.1	22.1	18.3	2.8

Notes: For companies who responded "should reduce scope & amount," and "opposed to tax." Numbers may not add up to 100 due to incomplete responses.

Nisay Business Conditions Survey

Survey date: August 2003

Sample size and composition: 2,308 companies, as shown below

① By company size

	No. of companies	Composition (%)
Large	191	8.3
2nd-tier	683	29.6
Small & medium	1,425	61.7
No response, other	9	0.4
Total	2,308	100.0

Note: Large companies have over 1,000 employees; 2nd-tier companies have 301- 1,000; small & medium companies have up to 300.

② By region

	No. of companies	Composition (%)
Hokkaido	113	4.9
Tohoku	151	6.5
Kanto	507	22.0
Koshinetsu, Hokuriku	64	2.8
Tokai	350	15.2
Kinki	596	25.8
Chugoku	267	11.6
Shikoku	118	5.1
Kyushu	110	4.8
No response, other	32	1.4
Total	2,308	100.0