
Setting up a business presence (a legal-entity) in Japan

A foreign company can set up a business presence in Japan in any one of following 4(four) formats:

- Representative Office
- **Branch Office**
- **Subsidiary Company** (Kabushiki-Kaisha or Godo-Kaisha)
- Limited Liability Partnership (LLP)

However to engage in commercial business activities in Japan the practical option is either to establish a “**branch office**” or a “**local subsidiary company**” as a legal entity.

Representative Office:

Representative office is generally established for carrying out market research & liaison activities on behalf of head office. It does not allow to conduct commercial business activities in Japan and **therefore no registration is required at the legal affairs bureau** nor be subjected to corporate tax under Japanese tax laws, except banking, security or similar businesses.

Branch Office

The simplest mode for a foreign company to establish a legal entity for commercial business operations in Japan is to set up a Branch Office. In terms of the range of business activities allowed, there are no basic differences between branch office and domestic corporations. Taxed on branch office income only and the rate is same as local co. For registration there is no requirement to establish statutory officers / management body, it only needs a **local physical address** (not a PO Box) & a **Representative in Japan** (must be a “**Resident in Japan**”). In general, transfer of operational funds between the branch and its head office can be made without restrictions, and is not subject to withholding tax. Branch can register max. 2 (two) “Representative in Japan” but one must be a “**Resident in Japan**” & in addition a director / member of the parent co. with his / her personal overseas resident address.

Subsidiary Company

A foreign company willing to establish a subsidiary company may choose from the followings:

- (a) **Kabushiki-Kaisha** [K.K. Co.] (Joint-stock corporation) {*Kabushiki Joto Seigen Kaisha – (If No Committee is Established)*}
- (b) **Godo-Kaisha** [G.K. Co.] Limited Liability Company (LLC) or similar entity stipulated by Japan's Companies Act.

There are also formats such as unlimited partnerships (Gomei-Kaisha) and limited partnerships (Goshi-Kaisha) under the Companies Act, but they are rarely chosen in practice because equity participants burden unlimited rather than limited liability.

A subsidiary co. is a separate legal entity from the foreign parent co., therefore foreign company will bear the liability of an equity participant stipulated by law for all debts and credits generated by the activities of the subsidiary co. Minimum requirement for establishing a subsidiary co in Japan is to have a **local physical address** (not a PO Box) & a local “**Resident in Japan**”. [Please see the “**Note(a)**” below re a local “**Resident in Japan**”.]

*Please see “**Note**” below re exception allowed for “subsidiary co.” since the change of regulation effective Mar'15.*

Limited Liability Partnership (LLP)

This format also allows to do business by using a **Yugen Sekinin Jigyo Kumiai**. It is considered as a **Japanese version** of a **limited liability partnership (LLP)**, it is **not a corporation, but a partnership** formed only by the equity participants, who have limited liability. Taxes are levied on profits allocated to equity participants but no tax on LLP. The format is normally used for carrying out a time bound project. One partner must be a local **"Resident in Japan"**.

Option re formation of a legal business entity in Japan for ongoing commercial activities:

The option is either to establish a **"Branch Office"** or a local **"Subsidiary Co. (Kabushiki-Kaisha or Godo-Kaisha)"**.

Note(a) re a local **"Resident in Japan"**: Either a Japanese or a foreign national, but in case of a foreign national the person must have an appropriate status of residence as per immigration law.

"Note" re exception allowed for "subsidiary co." since the change of regulation effective **Mar'15**.

Japanese govt. has allowed foreign co. to register a local **subsidiary co.** in Japan without a local "Resident in Japan". [*In case of G.K. Co. the overseas investor must be a corporation*]

But in both cases it would require a temporarily a local **"Resident in Japan"** for the purpose of completing the procedure of paid-up capital for K.K. Co. & equity participation for G.K. Co. In case of a **K.K. Co.** a "local resident shareholder" & in case of a **G.K. Co.** a "local resident member (equity holder)".

- Local resident's personal bank account is used for paid-up capital / equity procedure for registration purpose.
- Once the registration is completed the local resident's token share / equity is transferred back to the overseas investor through an internal co. document duly endorsed by both parties.
- However, in the **"Notification to Bank of Japan"** the share / equity participation at the time of registration shall be reflected & it cannot be amended post-registration.
- The reflection of 100% investment by the foreign investor shall reflect on the company tax-return document once the first company tax return is filed to the tax authorities.

Some other related matters for reference: [*For subsidiary co. without a "local "Resident in Japan"*]

- ❖ Re opening Co. Bank a/c: For past several years opening an "ordinary bank a/c" (Futsu Koza) even for local co. owned by local citizen or resident has become stringent. Usually it takes about two(2) weeks for bank to check & evaluate the docs & to convey their final decision at their discretion. So far for a foreign owned subsidiary co. with a "local resident in Japan" on board going through the same process with further scrutiny but with all required docs in place mostly received favorable decision!
- ❖ However, for the subsidiary co. registered without a local **"Resident in Japan"** under the new regulation does not seem to be getting the same treatment as mentioned above. It appears that local banks are not on the same page with the Japanese govt. when it comes to the new co. regulation effective Mar'15. According to news article published in the past it seems that Japanese govt. wanted to make it more flexible for foreign co. to open a subsidiary co. in Japan & with regard to Co. Bank a/c perhaps thought

that these companies even can operate business in Japan by opening a overseas bank a/c in the name of the subsidiary co. in Japan!

- ❖ Re the perception of local business partner(s) and or client(s) in Japan doing business with a foreign owned subsidiary co. without any local resident director / executive officer is a matter to be kept in mind! This issue would going to vary case by case depending upon the new co.'s purpose, activities & their business contacts (including proposed business contacts) in Japan!
- ❖ The above points are for reference only.

Some Basic differences between Opening a Branch and Establishing a Domestic Corporation in Japan

In terms of the range of business activities allowed, there are no basic differences between branch office and domestic corporation. But regardless of the firm being foreign or not, some companies, depending on the category of business, are required to secure authorization of the supervisory ministries at the time of founding after the registration.

A Branch office is not regarded as an independent legal entity, but as acting on the basis of decisions and instructions from the parent company (head office) to provide services and carry out business activities, including purchasing, importing, and sales etc. In transactions with other businesses, the branch office concludes contracts as the representative of its parent company (head office).

Some major differences between a branch office and A domestic Japanese corporation

Either a branch office or a domestic corporation may enter into business activities by its own name as an entity. Tax rates are also fundamentally same for a branch office and a domestic corporation. However, the major differences are in the following areas:

- 1) A new management body need not be set up for a branch office and there is no detailed statutory requirement for the management of a branch office. While a domestic corporation must have statutory officers or a management body such as directors, auditors, board of directors meetings and shareholders meetings, a branch does not require to do so but only needs a Representative in Japan.
- 2) Dividends paid by a domestic corporation to a foreign shareholder are subject to withholding tax, while remittance of branch profits after tax to its head office is not subject to withholding tax.
- 3) Expenses incurred by the head office for its branch may be allocated to its branch if it is spent for branch purpose.
- 4) Interest or royalty paid by the head office for activities of its branch, may be deducted by its branch although such interest or royalty is subject to withholding tax.
- 5) Local "Resident in Japan": Branch must have a "local resident in Japan" out of the max. two "Representative in Japan" that is allowed for registration. However, in case of a local "subsidiary co." under new law effective Mar'15 it is no more mandatory to have "a local "resident" director" in case of K.K. co. & "Member / Executive Officer" in case of G.K. co. But in case of a G.K. co. the investor must be an overseas corporation! (But subsidiary co. need a "Resident in Japan" temporarily for registration)

Comparison between Japan “Branch Office” and “Subsidiary Co.”

| | Branch Office | Subsidiary Company | |
|---|--|--|---|
| | | Kabushiki-Kaisha {(Kabushiki Joto Seigen Kaisha) (If No Committee is Established)} | Godou-Kaisha Limited Liability Co (LLC) |
| Capital | No capital (same as HO) | 1 yen or more (*1) | 1 yen or more (*1) |
| Number of investors | Not applicable | 1 or more | 1 or more |
| Liability of equity participants / parent co. toward creditors | <i>Unlimited</i> | Limited to amount of equity participation | Limited to amount of equity participation |
| Transfer of equity participation share | <i>Not applicable</i> | May be transferred freely in principle. May be stipulated in articles of incorporation so that approval of Board of Directors is needed for transfer of shares. | Unanimous approval of equity participants (members) required |
| Number of executives required | <i>Representative in Japan - 1 or 2(*2)</i> | Appointment of 1 or more (*2) . Representative director with right to execute business. If no representative director is appointed, executive officers each have the right of representation. | No legally stipulated min. In principle, all members are executive officers, but a representative member may be appointed (*2) . |
| Legally stipulated term of office for executives | <i>No legally stipulated term</i> | 2 years in principle. Extendable up to 10 years | No legally stipulated term |
| Regular general meeting of shareholders / members | Not required | In principle, must be held every year | Not required |
| Possibility of public offer of stock | Not applicable | Possible | Not possible |
| Possibility of reorganization into joint-stock corporation | Not possible. Need to separately close branch office and establish joint-stock corporation (*3) | N/A | Possible |
| Distribution of profits and losses | C/o Parent Co. | Allocated according to equity participation ratio | May be allocated at a different ratio from equity participation ratio if specified in articles of association |
| Taxation of profits | Income arising within Japan is in principle taxed | Taxed on profits according to a K.K. Co and profits allocated to shareholders | Taxed on profits according to a G.K. Co and profits allocated to members |

(*1) Establishment with zero yen capital is theoretically possible but in practice to incorporate without paying capital is not possible.

(*2) At least one representative must be a “Resident in Japan”. [Except for subsidiary company under new regulation effective Mar’15, however in case of a G.K. Co. in such case investor must be an overseas company]

(*3) Refer to "Closure of branch office" for details.

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Comparison between Japan K.K. Co. and G.K. Co.

| | K.K. Co. (Kabushiki Joto Seigen Kaisha) [If No Committee is Established] | G.K. Co. (Godo-Kaisha) [Limited Liability Co] LLC |
|--|---|---|
| Transfer of equity participation share | May be transferred freely in principle. May be stipulated in articles of incorporation so that approval of Board of Directors is needed for transfer of shares. | Unanimous approval of equity participants (members) required |
| Number of executives required | Appointment of 1 or more required. Representative director with right to execute business. If no representative director is appointed, executive officers each have the right of representation. | No legally stipulated minimum. In principle, all members are executive officers, but a representative member may be appointed. |
| Legally stipulated term of office for executives | 2 years in principle. Extendable up to 10 years | No legally stipulated term |
| Possibility of a Company to be a Director | Not possible | Possible. However, the co should nominate an individual staff from the co. |
| Director must be from shareholder /member | Not necessarily | In principle, all members are executive officers, but may be stipulated otherwise in "Articles of Association" |
| Regular general meeting of shareholders / members | In principle, must be held every year | Not required |
| Possibility of public offer of stock | Possible | Not possible |
| Possibility of reorganization | A joint-stock corporation (KK) may be reorganized into a limited liability company (LLC) (GK). | A limited liability company (LLC) (GK) may be reorganized into a joint-stock corporation (KK) |
| Distribution of profits and losses | Allocated according to equity participation ratio | May be allocated at a different ratio from equity participation ratio if specified in Articles of Association |

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Comparison of different types of legal business entity in Japan

Foreign companies or individuals generally engage in business operations by establishing a branch office, subsidiary company, or limited liability partnership, and the legal differences between each of these are summarized in the following table.

| | | Subsidiary Company | | Partnership Business |
|---|--|--|--|---|
| | Branch Office | Kabushiki-Kaisha (K.K. Co.) (Joint-stock Corporation) {(Kabushiki Joto Seigen Kaisha) (If No Committee is Established)} | Godō-Kaisha (G.K. Co.) Limited Liability Co (LLC) | Limited Liability Partnership (LLP) |
| Restrictions on equity participation | Notification not required with the Bank of Japan (Except certain industries) | Notification must be filed to the Bank of Japan | Notification must be filed to the Bank of Japan | Notification not required with Bank of Japan (Except certain industries) |
| Capital | No capital (same as HO) | 1 yen or more (*1) | 1 yen or more (*1) | 2 yen or more (if 2 Partners) |
| Number of investors | Not applicable | 1 or more | 1 or more | 2 or more (*3) |
| Liability of equity participants / parent co. toward creditors | <i>Unlimited</i> | Limited to amount of equity participation | Limited to amount of equity participation | Limited to amount of equity participation |
| Transfer of equity participation share | <i>Not applicable</i> | May be transferred freely in principle. May be stipulated in articles of incorporation so that approval of Board of Directors is needed for transfer of shares. | Unanimous approval of equity participants (members) required | Unanimous approval of partners required |
| Number of executives required | <i>Representative in Japan - 1 or 2(*2)</i> | Appointment of 1 or more (*2). Representative director with right to execute business. If no representative director is appointed, executive officers each have the right of representation. | No legally stipulated min. In principle, all members are executive officers, but a representative member may be appointed (*2). | No legally stipulated min. All partners are executive officers (*3). |
| Possibility of a Company to be a Director | <i>Not applicable</i> | Not possible | Possible. However, the co must nominate a staff from the co. (*2) | Not applicable |
| Director /Executive must be from shareholder /member | <i>Not applicable</i> | Not necessarily | In principle, all members are executive officers, but may be stipulated otherwise in "Articles of Association" | Not applicable |
| Legally stipulated term of office for executives | <i>No legally stipulated term</i> | 2 years in principle. Extendable up to 10 years | No legally stipulated term | No legally stipulated term |
| Regular general meeting of shareholders (members) | Not required | In principle, must be held every year | Not required | Not required |
| Possibility of public offer of stock | Not applicable | Possible | Not possible | Not possible |
| Possibility of reorganization into joint-stock corporation | Not possible. Need to separately close branch office and establish joint-stock corporation (*4) | N/A | Possible | Not possible. Need to separately dissolve partnership and establish joint-stock corporation |
| Possibility of reorganization | Not possible. Need to separately close branch office and establish KK or GK (*4) | A joint-stock corporation (KK) may be reorganized into a limited liability company (GK). | LLP (GK Co) may be reorganized into a KK | Not possible. Need to separately dissolve partnership and establish a KK or GK Co. |
| Distribution of profits and losses | C/o Parent Co. | Allocated according to equity participation ratio | May be allocated at a different ratio from equity participation ratio if specified in articles of association | May be freely allocated with the unanimous approval of partners |



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|----------------------------|---|---|---|---|
| Taxation of profits | Income arising within Japan is in principle taxed | Taxed on profits according to a K.K. Co and profits allocated to shareholders | Taxed on profits according to a G.K. Co. and profits allocated to members | No taxation on LLP. Taxation of profits allocated to partners |
|----------------------------|---|---|---|---|

(*1) Establishment with zero yen capital is theoretically possible but in practice to incorporate without paying capital is not possible.

(*2) At least one representative must be a "Resident in Japan". [Except for subsidiary company under new regulation effective Mar'15, however in case of a G.K. Co. in such case investor must be an overseas company]

(*3) One or more partner must be an individual who has an address in and is resident in Japan for more than 1 year, or a Japanese corporation.

(*4) Refer to "Closure of branch office" for details.

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