Aoyama Sogo Accounting Firm Innovation Speed Quality

NewsLetter

Aoyama Sogo Accounting Firm

Vol.25 8/31/2023

Chairman's Column

Extended terms for a longer life — Mortgages are now 50 years

I hope you are doing well even with the high temperatures and consecutive typhoons coming through. As residential property prices continue to rise, an unexpected financial product has arrived.

SBI Sumishin Net Bank announced that their repayment period on mortgages will be extended from 35 to 50 years. The aim is for young people to easily purchase property. Although I am surprised with the term of 50 years, perhaps with a 100-year life and longer employment period on the horizon, it will be interesting to see whether this product can stand the test of time.

As an administrator of securitized mortgages, Aoyama Sogo is paying close attention. In describing our company and securitization business to new hires, I joke that the "longest mortgage is 35 years. Of course, I likely won't be around in 35 years." It's really mind-boggling to think this will become 50 years.

The advantages include a lower monthly repayment. With a 50-year term, the monthly repayment will be reduced. It will give young people a greater chance to purchase property by reducing their economic burden. Additionally, by reducing their monthly repayment, it will improve their current finances and allow them to invest in their career.

As for disadvantages, there is the risk of default midway through the term. The product description states, "for clients that have stable and continuous income." However, with life-time employment systems that may vanish, even if current income levels are sufficient, the requirement may be harder to meet in the future.

It is difficult to accurately predict Japan's economy in 50 years. For instance, 35 years ago, in 1988, Japan was in a bubble economy. For those that agreed to a 35-year mortgage, who would have thought Japan would face the lost 30 years, deflation, and the current ultra-low interest rate climate? In the past, there were historical events like the myth of ever-increasing land prices, the New York terrorist attacks, Lehman Brothers fallout, and the Great East Japan Earthquake.

It's hard not to be concerned about the current state of affairs including the Russian-Ukrainian War and heightened geo-political risks between the U.S. and China. With a longer repayment period, risks increase in relation to future interest rates and economic changes. It's important to factor in such uncertainties in one's plan.

The younger generation often uses subscription services and values cost-effective and time-efficient products, so it's up to the individual to select products that fit their lifestyle and future outlook. Also, with remote work and workcation gaining validity, commuting to the city may be becoming less common for society.

In either case, I hope these new products can give new opportunities for younger generations to live better.

by Kazuhiro Matsuzawa, Chairman

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Japan Business

The Regulatory Sandbox in Japan
- Obtaining special exemptions

On August 1, it was reported that Ownership Co., Ltd., a subsidiary of Digital Securities Preparatory Co.,Ltd. obtained approval for its “New business activity plan” for an ST (security token) system that digitally secures protection from third party claims under a “GK-TK structure”. To secure protection against third party claims, the use of a Japanese Depositary Receipt (structure for beneficiary certificate for entrusted securities) seems to be common, but in the future the use of a “GK-TK structure” as an alternative may spread.

What exactly is a “New business activity plan”? The “Regulatory Sandbox” was introduced under the Act on Strengthening Industrial Competitiveness to ease regulation for new technologies such as fintech, blockchain, and mobility. The Act provides special exemption for approved projects.

For companies that seek to operate under eased regulation, the “sandbox” is used by participants for a limited time to reach proof of concept. Based on the results, the Japanese government approves a special exemption that eases regulation. Since the system began in 2018, 30 projects and 149 companies have been approved.

Recently, electric kickboards have been seen on the street. Luup, the start-up behind it, obtained approval in 2019 and began the rental kickboard business. Among the companies that have applied, some have received approval for special exemption at a remarkable speed of less than a year after submitting their business plan. The “sandbox” modeled after the England version initially faced skepticism on its effectiveness. It now appears that implementation is steadily on the rise.

A while ago when I was doing structuring at a financial institution, the setup of a new structure would require enormous time and effort to stay within regulations. Since regulations were a given, opinion letters from law firms, tax firms, and accounting firms had to be obtained as well as the related government official’s “opinion”. It’s almost like a dream that special exemptions are now approved to ease regulation. It’s often said that “the easement of policies is very slow in Japan”, so companies should take advantage of systems like this.

by Shigeru Hirai, Client Relations Group

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Japan Investments

【New NISA】
Nippon (Japan) Individual Savings Account

With the 2023 Tax Reform, tax exemption for small investments (New NISA) for individuals will begin. It is central to the government's aim of shifting "savings to investment." Compared to the current NISA, it has the characteristics outlined below.

Many individual investors are expected to open a New NISA account to take advantage of the unlimited tax exemption period and increase in annual investment limits and maximum allowable investment. Additionally, the maximum allowable investment is replenished when investments are sold. For example, if stocks are purchased at 1,000,000 yen within the growth investment limit and sold at 1,200,000 yen, the 200,000 profit is not only tax-exempt, but in the following year, the maximum allowable investment is replenished by 1,000,000 yen. This means that repeated investments are now possible.

With regards to replenishing the maximum allowable investment, the Financial Services Agency is aware of the possibility that brokers/dealers may solicit short-term reinvestments to gain service fees. It has stated that disciplinary action will be taken against malicious solicitors of churning.

Also, monthly distribution-type index funds that are popular among the elderly are excluded from growth investment products because the distribution withdraws a portion from principal (known as "excess distribution") and determined unsuitable for long-term investment (investable products available under the reserve investment limit is equivalent to the current reserve NISA). To work around this exclusion of the monthly distribution-type, there seems to be similar types of index funds that invest on even and odd months that substantially result in a monthly distribution.

I do hope that brokers and investment managers sell and manage products that assist individuals in building wealth, but ultimately the individuals that make the investment should fully understand the products and utilize NISA for wealth creation.

by Jun Yoshioka, ASA Advisory

	New NISA	Current NISA
Combination of types	Combining reserve and growth investment limits is allowed	Either Reserve NISA or General NISA
Tax exemption period	No limit	Reserve NISA: 20 years General NISA: 5 years
Annual investment limit	Reserve investment limit 1,200,000 yen Growth investment limit 2,400,000 yen	Reserve NISA 400,000 yen General NISA 1,200,000 yen
Maximum allowable investment	Total investment 18,000,000 yen (of which maximum growth investment 12,000,000 yen)	Reserve NISA 8,000,000 yen General NISA 6,000,000 yen
Investment limit for sold investments	Max allowable investment amount is replenished and reusable in following year and afterwards	Sold investments do not replenish the max allowable investment amount

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Japan Tax Update

[Tax savings on High-rise Condos] Reform proposal announced for Inheritance tax assessment of Condos

The National Tax Agency announced a new calculation method for assessing condo values for inheritance tax called the "Notice of (proposed)interpretation of law for assessment of residential category assets", open for public comment from July 21.

Previously, there were many cases where the condo's assessed value based on the Circular for property valuation differed substantially from market price. For condos, that variance was obvious, and the National Tax Agency began to pay closer attention to excessive "tax savings on high-rise condos."

According to the National Tax Agency sample survey (from 2011 to 2013 of condo sales at least 20 floors high), the variance between assessed inheritance tax value and market price (market price/inheritance tax value) was at most 6.93 times and on average 3.04 times. Additionally, a separate National Tax Agency survey (of condo sales from 2013 to 2015) revealed that average variance was 2.34 times with about 65% of condos having an inheritance tax value less than half of market price.

In principle, inheritance asset value is based on the Circular for property valuation. However, uniform application of the circular may result in inappropriate valuation, thus section 6 of the circular prescribes an exceptional valuation method. Resultingly, high-rise condos had already carried the risk that the assessed value is deemed unreasonable. However, moving forward, all condos are expected to be subject to the reform of valuation method for inheritance tax.

As stated on the next page, the **<Reform proposal>** is expected to apply to inheritance, bequest, or gift from January 1, 2024, and onward with the change that a specified "adjustment ratio" will be applied. The "adjustment ratio" is based on building age, number of floors, floor level of unit, and ratio of land use right of unit to exclusive floor area. I will omit the details but for example, an older building will have a lower value, and a building with more total floors will have a higher value. Under the reform proposal, the inheritance tax value of a condo will be about 60% of theoretical market price at minimum, and in some cases may be double the current assessed value. Additionally, apartment buildings with one owner and condos sold by real estate firms will be excluded under the reform proposal.

The new reform will have a big impact on the use of condos in inheritance tax planning, so it is wise to pay close attention to upcoming developments.

by Sachie Aoki, Tax Consulting Group

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Japan Tax Update

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<Reform proposal>

Assessed value of one condominium unit:

① Price of separately-owned building unit + ② Land (land use right) price

	Current	Reform proposal
① Price of separately-owned building unit	Property tax value of building[※2] x 1.0	Property tax value of building[※2] x 1.0 x <u>Adjustment Ratio</u>
② Land (land use right) price	Price of entire land[※3] x Co-ownership share (land rights ratio)	Price of entire land[※3] x Co-ownership share (land rights ratio) x <u>Adjustment Ratio</u>

※1 Section 6 of the Circular for property valuation (If valuation in accordance with the circular is difficult). If valuation in accordance with the circular is recognized as grossly inappropriate, the National Tax Agency Commissioner will give instructions on valuation.

※2 Calculate property value by prorating the entire building value by the portion of exclusive floor area.

※3 Calculate value by roadside land value method or multiplier method.