

Consumption tax implication for Cross-border Supplies of Services

For foreign businesses

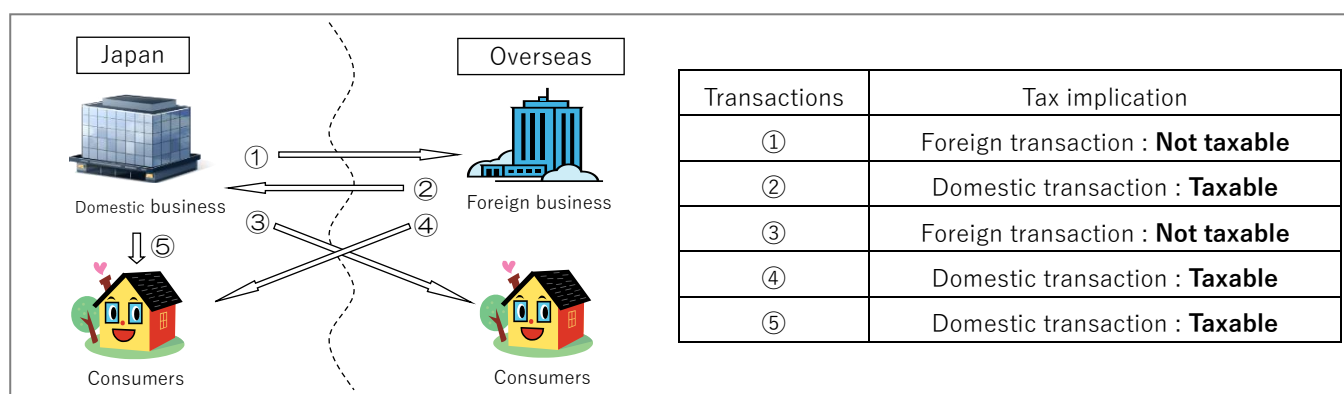
National Tax Agency, July 2024

I Criteria for determining either domestic or foreign transactions with regard to provision of electronic services

Regarding the provision of services via telecommunication lines (Internet, etc.) such as providing digital content of books, music tunes, advertising messages, etc. (hereinafter “provision of electronic services”), whether they are the domestic transactions subject to taxation of consumption tax or not needs to be determined based on the “whereabouts, etc. of those who receive the provision of the services*” (domestic vs. foreign determination).

Taxation relationships relating to provision of electronic services are as follows, depending on those who provide the services as well as on those who receive the services.

* Domicile or residence for individuals; and location of the head office or the main office for corporations.



Among B2B electronic services received by a foreign business at its “permanent establishment”*, if the services are required for the transfers of assets conducted in Japan, they are regarded as domestic transactions. (subject to a “Reverse charge mechanism”)

Among B2B electronic services received by a domestic business at its “place of business or the like outside Japan”*, if the services are required only for the transfers of assets conducted outside of Japan, they are regarded as foreign transactions. (not subject to a “Reverse charge mechanism”)

* These refer to “permanent establishments” or “the places of business or the like outside Japan” under Income Tax Act or Corporate Tax Act.

Key points

- Whether transactions are domestic or foreign is determined if the address of the electronic service recipient is in Japan.
- Whether the address is in Japan shall be determined based on objective and reasonable criteria, for instance by comparing the location of the address presented by a customer via internet with “country of issue” information in a credit card by which a customer settles payment. As such, the location of address is determined by reasonable and objective methods in accordance with the nature of each transaction.

○ What is the “provision of electronic services”?

The “provision of electronic services” covers advertising on the internet and providing cloud services as well as consulting business via telephone and email in addition to provision of e-books, music, and software via telecommunication networks.

Electronic services do not include the provision of services that mediates other people’s telecommunications using telephone, telegraph, and other telecommunication equipment—in other words, use of telecommunication networks such as telephone, FAX, and access to the internet.

Electronic services also exclude services notifying the results of transfer assets via telecommunication networks when the notification is ancillary to other transfer assets.

Examples of transactions covered by the “provision of electronic services”

The provision of electronic services covers for instance the following transactions when these transactions involve payment for services:

- Provision of e-books, digital newspapers, music, videos, and software (including various applications such as games) via internet
- Services that allow customers to use software and databases in the cloud
- Services that provide customers with storage space to save their electronic data in the cloud
- Distribution of advertisements via internet
- Services that allow customers to access shopping and auction sites on the internet (e.g., charges on posting goods for sale, etc.)
- Services that allow customers to access the place to sell game software and other products on the internet
- Provision via internet reservation website for accommodation and restaurants (those who charge on posting for the website from the businesses that operate accommodation and restaurants)
- English lessons provided via internet

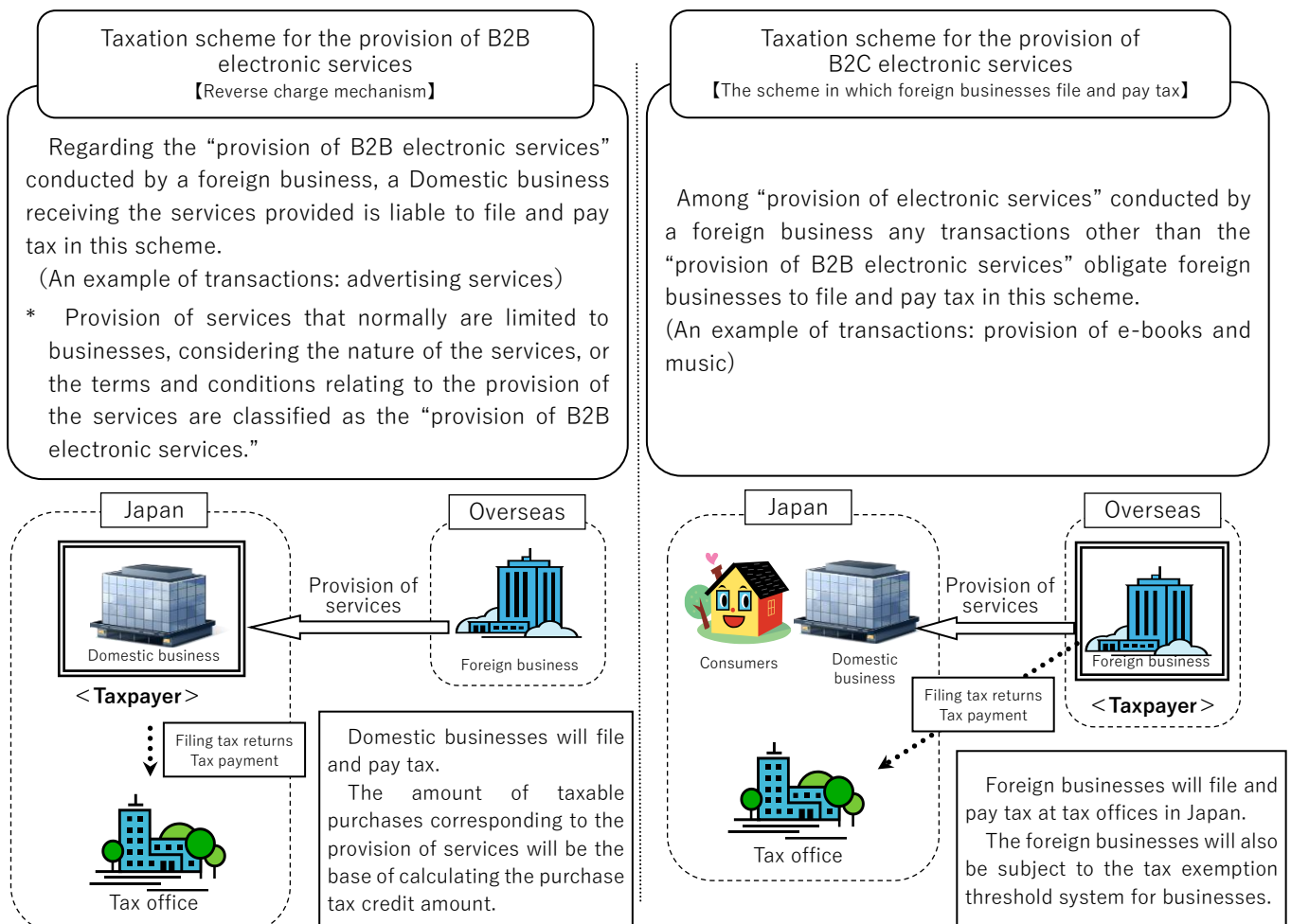
Examples of transactions that do not fall under the “provision of electronic services”

Use of telecommunication networks and transactions where services via the telecommunication networks are ancillary to the transfer of other assets do not fall under the provision of electronic services. Examples are as follows:

- Services merely mediate information transmission among subscribers (so called telecommunication) , such as telephone, FAX, telegraph, data transmission, and access to the internet
- Software development, etc.
 - * One may request a foreign business to create a copyrighted work and then give instructions during the development process or receive the final products via internet. The use of the internet, in this case, is ancillary to a copyrighted work; therefore, this transaction does not fall under the provision of electronic services.
- Administrating and managing assets outside Japan (including Internet banking services)
 - * Even if the internet is used to give instructions regarding asset management or fund transfer, and to report on its status or results, the use of the internet, in this case, is ancillary to the administration and management of assets; therefore, this transaction does not fall under the provision of electronic services. However, if one receives, for example, a charge for the use of asset management software in the cloud, this part comes under the provision of electronic services.
- Requesting foreign businesses to collect and analyze information, etc.
 - * Reported via internet, the use of the internet, in this case, is ancillary to collecting and analyzing information; therefore, this transaction does not fall under the provision of electronic services.
However, if one collects and analyzes any information without being requested to do so by other businesses and he/she makes publicly available or provides it via internet with fees being charged for the services, this transaction comes under the provision of electronic services.
- Foreign legal professionals pursuing litigation outside Japan
 - * Even if the internet is used to report status or to instruct on litigation, the use of the internet, in this case, is ancillary to pursuit of litigation outside Japan; therefore, this transaction does not fall under the provision of electronic services.

II Taxation scheme for the provision of electronic services

When electronic services are provided by a foreign business, a taxation scheme is decided depending on the service provided either being the “provision of B2B electronic services” or the “provision of B2C electronic services” as follows:



○ What is “provision of B2B electronic services”?

Among provision of electronic services conducted by foreign businesses, “provision of services that normally are limited to businesses, considering the nature of the services, or the terms and conditions relating to the provision of the services” are classified as the provision of B2B electronic services.

Services classified as the “provision of B2B electronic services” considering the nature of the services are, for instance, the distribution of advertisements on the internet and the provision of market-places to sell application software including games at the websites on the internet.

Services classified as the “provision of B2B electronic services” considering the terms and conditions are, for instance, among provision of electronic services such as cloud services that are individually negotiated between parties involved in the transaction, whereby a particular contract is concluded between the parties, and are on the contract obviously intended for business use by the business receiving the services.

On the other hand, for example, if cloud services which a service provider accepts applications from a customer at the websites on the internet, state with notice that “this service is for business use”, but if the service provider cannot effectively restrict these applications from consumers and others those who are not in businesses, such services do not fall under the “provision of services that normally are limited to businesses” from their terms and conditions.

Accordingly, such transactions are classified as the provision of B2C electronic services, obligating foreign businesses providing the services to file and pay tax.

【Note】Notification duty of a foreign business providing the services that are subject to the reverse charge mechanism

“Provision of B2B electronic services” and “provision of specific services” received domestically from foreign businesses (see V) are called “specific taxable purchases,” and the domestic businesses that received the provision of the services are supposed to file and pay the tax concerning the “specific taxable purchases” (reverse charge mechanism).

In this case, a foreign business providing the services that fall under “specific taxable purchases” must notify in advance that the transactions are subject to the “reverse charge mechanism” (the business who receives the provision of the services is liable to pay consumption tax on the “specific taxable purchases”).

As for how to notify, the point needs to be notified to the transaction counterparties in manners they can easily recognize it: for instance, post it on the place where the transaction details are introduced over the Internet; describe it in the communication documents in case transaction details are negotiated individually, etc.

○ What is “provision of B2C electronic services”?

The provision of B2C electronic services covers those such as the following transactions:

- Provision of e-books, music, and videos that is generally provided for consumers;
- Services that state on a website that they are intended for business use, but that cannot effectively restrict applications from consumers and others those who are not in businesses.
- * The “provision of B2C electronic services” is not limited to services that only consumers receive but also include services received by businesses.

【About tax return by a business “providing B2C electronic services”】

When a foreign business provides B2C electronic services, the foreign service provider is liable to file and pay tax (excluding the items that are subject to the platform taxation [see below]).

Reference

○ Exemption threshold for businesses

In principle, a business with taxable sales not exceeding 10 million yen in the base period for the taxable period is exempt from consumption tax obligation.

For example, if a foreign business provides electronic services only, its taxable sales would be the sales amount associated with B2C electronic services for provided within Japan.

The taxable sales do not include sales associated with the provision of B2B electronic services.

- * For the taxation periods starting on October 1, 2024, or beyond, whether a foreign business is liable to pay tax or not cannot be determined by the total amount of salaries, etc. paid. See the “Notification on the Revision of the Consumption Tax Act (April 2024)” for details. (Only in Japanese)

○ Designation of a Tax Agent

A sole proprietor without domicile or residence in Japan and a corporation without a head office or an office in Japan are required to designate a Tax Agent to deal with submission of tax returns and notification documents, and tax payment.

【About the platform taxation】

The tax reform of FY2024 prescribes the following will take effect on April 1, 2025: regarding the B2C electronic services that are provided by foreign businesses using a digital platform and for which prices of the services provided are collected via a specific platform business (that is, a platform business designated by the Commissioner of the NTA, as satisfying certain requirements), the specific platform business is liable to file and pay tax assuming that the provision of the services was done by the specific platform business (platform taxation).

See the “Platform taxation for consumption tax” on the website of the NTA, for details.

* Regarding the provision of B2C electronic services which is not subject to the platform taxation, the business that provides the services is liable to file and pay tax.

III About the purchase tax credit associated with B2C electronic services provided by foreign businesses

The businesses that received the “provision of B2C electronic services” by foreign businesses need to retain the qualified invoices (including the electronic records on the items described in the qualified invoices) issued by the sellers = foreign businesses, when applying the purchase tax credit to the services.

Therefore, any foreign business that pursues “provision of B2C electronic services” needs to consider becoming a business issuer of qualified invoices, based on its business content (sales destinations, etc.).

【About the transactions subject to platform taxation】

In case provision of B2C electronic services by a foreign business is put subject to the platform taxation on April 1, 2025, or beyond, provision of the services will be regarded as what was done by a specific platform business. Therefore, the qualified invoices that will be necessary for the business, that received the provision of the services, to apply the purchase tax credit, will be issued by the specific platform business. Therefore, even if the foreign business is a business issuer of qualified invoices, the foreign business will not be liable to issue qualified invoices.

See the “Platform taxation for consumption tax” on the website of the NTA, for details.

IV About registration of business issuers of qualified invoices

If a foreign business wants to get registered as a business issuer of qualified invoices, it needs to submit an “application for registration as a business issuer of qualified invoices (for a foreign business)” to the District Director of the Tax Office covering the tax payment place.

In addition, any business that was registered as a business issuer of qualified invoices becomes a taxable business irrespective of the taxable sales amount of its reference period. Getting registered or not per se is entirely up to each business.

Regarding the details of registration requirements, procedures, etc. for a business issuer of qualified invoices, see the special corner for the invoice system on the website of the National Tax Agency.

V Consumption taxation scheme for services related to entertainment and sports provided by foreign businesses

When a foreign business provides transaction as a business main content of which is to provide services by film or theater actors/actresses, musicians, and any other entertainers, or professional athletes, and the service is provided by the foreign business to other businesses, the transaction is regarded as a “provision of specific services.”

When the “provision of specific services” is conducted by a foreign business for a business, the business receiving the service is liable to file and pay tax on the specific taxable purchases for receiving the specific services (a reverse charge mechanism).

Details are available in “Revision of a consumption taxation scheme for services related to entertainment and sports provided by foreign businesses” on the NTA website. (Only in Japanese)

- Contact your nearest tax office for any questions or further details.
- Those who would like to consult with a tax officer in person (for cases that require confirmation of actual specific situations with relevant documents) will need to arrange a reservation for an interview by telephone in advance. Your cooperation is appreciated.