

A Study on the Asset Management and Taxation Types of the Rich in Japan

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Abstract: The Japanese economy is facing a new phase from a long-term recession over the past 30 years to an annual economic growth of around 2%. With the recovery of the Japanese economy, not only foreigners but also Japanese capital are returning to Japan. Already, the Japanese Composite Stock Price Index has exceeded 39000 points before the bubble burst. Changes in the yen exchange rate are also inducing the inflow of foreign capital into Japan. In this economic trend, investors are paying attention to the Japanese capital market, and in particular, the wealthy in Japan are focusing on the Japanese domestic market to increase their assets. In particular, the Japanese financial market is attracting attention as a relatively safe asset due to the unstable environment at home and abroad. According to this trend, asset management of the wealthy in Japan is also carried out in various ways. Sometimes there are considerable losses due to asset management failures. That is why it has emerged recently to use various tax savings. Companies and individuals show the same behavior. On the contrary, the government sometimes strengthens monitoring in various ways to prevent a decrease in tax revenue. This phenomenon has recently become common in Japan.

KeyWords: Japan's Wealthy; Wealth Management; Asset Growth; Tax Savings; Investment Types; Tax Avoidance

1. Definition of the Japanese Wealthy

Although there is no clear definition of the term wealthy, it generally refers to those who have a lot of money and assets, but it is not defined how much they actually have to have. According to the definition of the wealthy by the NOMURA General Research Institute in Japan, those who hold net financial assets (the sum of financial assets held by households, such as deposits and installment savings, stocks,

investment trusts, and life insurance, minus liabilities) are defined as those who hold more than 100 million yen and less than 500 million yen .

In Table 1, less than 30 million yen of net financial assets belong to the Mass layer, and in Japan, 78% of households belong to this class. Most of them can be seen as salary men belonging to the Mass layer. The characteristic of the Upper Mass layer, which salary workers want to take to the next level, is that they were originally the Mass layer, but their assets increased due to asset management. This includes groups that have inherited assets from their parents. Most of the Upper Mass's jobs are professional professions, and include lawyers, doctors, certified public accountants, high-level company officials, and foreign-funded employees. They are increasing their additional income from non-working income through stocks, bonds, and real estate investment. The characteristics of the Upper Mass layer and people at higher levels are, first, a strong health consciousness. They have a stronger health consciousness than the Mass layer. There is a consciousness that you must be healthy to not pay unnecessarily for hospital expenses. Second, thoughts are positive. Physical health soon leads to mental health. They are not afraid of failure, see a crisis as an opportunity, and accept it as an opportunity. Third, they judge their essential values. The basics of what is valuable in assets are clear. They are people who make a judgment by absolutely thinking about whether it will be beneficial to them or not, not the general evaluation of high value = value. If you are a Mass layer, you must first continue to increase your assets without reducing your accumulated assets to join the Upper Mass layer. They think that real estate is the answer to increasing assets. There is a strong belief that real estate is directed upward.

2. Status of Asset Growth

Meanwhile, due to rising interest rates, there

are many wealthy people who actively invest in dollar bonds to prepare for high exchange rate returns. However, as they also experienced investment failures, rising interest rates increased financing costs. Funds flowing from investment funds to venture companies also saw their profits plunge in the United States and other countries. IPOs, which had been booming so far, became difficult. IPOs are high

at 110 cases in 2022, but they declined in 2023. The rate of decline reached 17%. Whether it was a global financial crisis or a 32% decline in 2009, this has changed rapidly. Venture business managers tried for IPOs, but the number of companies selling companies canceled their listing plans due to deteriorating market environment.

Table 1. Status and Rate of Increase/Decrease of the Wealthy in Each Country

Ranking	City	the wealthy (people)	the super-wealthy(people)	Compared to 2012 Increase/decrease rate (%)
1	New York	340,000	724	40
2	Tokyo	290,000	250	Δ5
3	Bay Area	285,000	629	68
4	London	258,000	384	Δ15
5	Singapore	240,100	329	40
6	Los Angeles	205,400	480	35
7	Hong Kong	129,500	290	Δ27
8	Beijing	128,200	354	70
9	Shanghai	127,200	332	72
10	Sydney	126,900	184	35

Data: NOMURA Comprehensive Laboratory (2020) Reports on the Japanese Rich

Amid the fluctuations in the global financial market following the Corona epidemic, the wealthy preferred to invest in U.S. stocks. According to the representative stock index S&P 500, the average annual interest rate for 10 years until 2019 is more than 11%. If you hold an ETF (listed investment trust) linked with the same year for 10 years, the asset value will be about three times higher. From 2020, among U.S. stocks, there has been a lot of investment in high-tech stocks, including GAFAM. The Nasdaq Composite Index, which represents an indicator of high-tech stocks, has risen sharply to about 30% over two years, with the wealthy increasing their investment.

There was also a phenomenon that the wealthy avoided taxation due to changes in asset value. In 2021 ('July 2021 to 'June 2022), the amount of reported missing income per case of the wealthy reached 37.6 billion yen. It increased to 66% compared to the previous year. In particular, when limited to the wealthy doing overseas transactions, the amount of additional tax per case increased 3.3 times compared to the previous year. Compared to other general income tax additional taxes, the wealthy were found to be 9.1 times higher.

3. Type of Asset Growth

Asset management is the process of

maximizing profits and minimizing risk by operating the assets held by investors as efficiently as possible. The wealthy in Japan have been interested in asset management and investment in a variety of ways.

3.1 The Purchase of Dollar Bonds

At the end of the COVID-19 epidemic, the interest of the wealthy increased investment in US dollar bonds. In 2023, the number of consultations with the health partner corporation on US dollar bonds increased fivefold compared to the previous year. There are two main causes. The first is the high interest rate. The interest rate on US long-term bonds is 3.7% in the first half of 2022, the highest level in 12 years. When the interest rate on US bonds rises, interest rates on other bonds, such as bonds of US companies, inevitably rise. For that reason, even bonds with relatively high credit ratings of A and BBB received an interest rate of 5-6%. The second is the strong dollar. In 2022, the foreign exchange rate was around \$1 = 115 yen, but the dollar value rose to 151 yen in October of the same year due to the US interest rate hike.

3.2 Subordinated Bonds Abroad

Second, the type is subordinated overseas bonds. In a situation where interest rates are

rising, the dollar can receive higher interest than yen bonds. On the list of the 2024 National Securities Conference in Japan, dollar-denominated subordinated bonds issued by overseas banks are permanent subordinated bonds. Subordinated bonds are subordinated bonds to ordinary bonds when the issuing company goes bankrupt. Among them, permanent subordinated bonds have no fixed maturity, such as 5 or 10 years later. For that reason, the investment risk is high, so the interest is relatively high, but it is a dangerous product. There are 6-7 of these risk products, but there are bonds with high interest rates of more than 10%.

3.3 Structured Note

In 2023, the Japanese domestic market was confused. KOEI TECMO HOLDINGS, which develops game software, lost \$26 million due to investment in ATI bonds. Class action by the victim's wealthy also began to expand. What was noted is the issue of responsibility for securities companies to explain the risk of principal reduction clauses to some extent. According to the contract document, there are two conditions in the column below the principal reduction clause: when the ratio of CETI (Tier1 such as ordinary stock) is less than 7% (when accepting support from a processing agency). The latter (receiving support) does not seem to have a problem, but it is also true that the securities company that sold paid attention only to the CETI ratio. There was a lack of clear explanation even for the support from public institutions.

3.4 Real Estate Investment

Real estate has been recognized as a highly attractive product. This is because real estate is generally curved upward. Japan is no exception. For example, individual investors in houses were immediately resold without occupancy, whether used as an athlete's village for the Tokyo Olympics and Paralympics in Japan. The winning rate is 111 times the maximum magnification. The initial sale price was 50% higher than at the time of sale. Even considering the economic situation and taxes, the profit margin on sale was high.

3.5 A Boom In Senior Start-Ups

In 2022, the start-up boom weakened. This is

because financing costs increased as interest rate hikes continued due to global inflation caused by the outbreak of the COVID-19 pandemic. Therefore, the supply of start-up loans has begun to weaken rapidly. Most start-ups have become more and more difficult to list their stocks due to the high difficulty of financing for business abuse. In addition, what has come as a headwind is the issue of (trust-type stock option) (stock purchase right, SO). Although financing has become difficult or new tax problems have emerged, the entrepreneurial craze among the 60-year-old is increasing every year. In Table 1, a survey by Japanese policy and financial institutions surveyed the start-up plans for those interested in starting a business. 56.9% of the respondents who answered (starting a business within 10 years) and (want to start a business) were in their 60s, higher than 55.7% of those in their 20s and younger, which was the highest by age group. In the same survey in 2017, those in their 60s were 35.5%, the lowest by age group. It has risen by more than 20% in the last five years.

4. Types of Tax Savings for the Wealthy

4.1 Utilization of Depreciation

The wealthy are particularly interested in tax savings when their holdings decrease. For example, tax savings through the use of depreciation are increasing. The representative one is the use of lease. The use of lease was prohibited due to the tax amendment (2022). Nevertheless, the wealthy are using it a lot. Let's see why.

4.2 The Use of Life Insurance

Another aspect of the National Tax Service's increased monitoring is the avoidance of taxation with life insurance that has been widely used by small and medium-sized business owners in the past. Income is often hidden by receiving refunds for cancellation violations such as regular insurance. If the cancellation violation refund exceeds 1 million yen, the life insurance company must provide the payment details to the tax office. This had the effect of preventing income from being hidden.

4.3 Establishment of Public Interest Foundation

In principle, profits from public interest

foundations are not corporate tax. In addition, when property is donated to a public interest foundation, taxable income deducted from income is reduced, and inheritance tax is not levied on donated property, so listed companies often use the public interest foundation to reduce taxes. However, the original purpose of the public interest foundation is to contribute to society through 23 types of projects with high public interest, such as art and sports.

4.4 The Establishment of a Fund

However, establishing a public interest foundation takes a long time and requires directors and councilors. Therefore, establishing a public interest foundation is complicated and difficult. However, the fund can be established in about two weeks, resources are unnecessary, and all projects linked to social contribution are targeted. As a result, fund consultations of more than 100 million yen are increasing rapidly recently. With 5 million yen, you can establish your own fund, and assets other than cash, such as stocks and real estate, are possible. Those who wish to donate can talk to the foundation staff about the field or business they want to apply for and design the fund.

4.5 Hometown Tax Payment

The hometown tax payment is a law established to bridge the regional gap that began in 2008 in Japan, and is an area to be noted. In recent years, it is one of the donation tax systems aimed at bridging the gap in large cities, responding to tax reduction in population-reduced areas, and local development in an urban-intensive society. Donations to local governments are deducted as income tax or resident tax within the legally determined range. The presence of the wealthy in donations plays a big role in paying hometown tax. The amount of hometown tax paid is increasing every year. With the expansion of the market size, local governments are also interested in it.

4.6 Immigration Abroad

The pattern of overseas migration of the wealthy is changing. Until now, there have been many migrations for the inheritance measures of the elderly generation or for the purpose of education for the children of the active generation. However, if you acquire permanent residence, you are not obligated to

live and are not subject to inheritance tax. Migration is increasing for the purpose of avoiding taxation. Currently, the largest number of Japanese residents in the United States for more than 3 months including permanent residents is about 420,000, followed by China, Australia, Thailand, and Canada. In particular, immigration to Canada is increasing recently. This seems to have had an impact on foreign immigration policies due to the Canadian government's lack of skilled personnel in the fields of medical care and construction. The image of a country tolerant of foreign immigration served as a factor in increasing the immigration of the wealthy in Japan.

5. Strengthening the Prevention of Tax Avoidance

5.1 Increased Surveillance of Lease Utilization

The wealthy are trying to save tax, but the government is strengthening its prevention of tax avoidance. The end of the settlement period is March. The tax saving method is to use profits during this period in settlement measures. The important thing is to use it as a loss (cost) cost of small depreciable assets such as small leases. This is to keep the tax burden low, with the total cost of the lease being spent at one time as a loss cost.

The income of the wealthy has a relatively large proportion of financial income such as stock investment. Salaries and business income are comprehensive taxation, and the maximum tax rate is 45%. Meanwhile, financial income is a separate tax, and the tax rate is about 20%. The higher the ratio of financial income, the lower the burden rate. Considering the fairness of the tax burden, it should be improved to be wrong.

However, introducing a new system such as the Japanese consumption tax is unlikely. Although it is not easy considering the opposition of the wealthy, many of the wealthy will be affected by lowering the level of personal income after 2024.

5.2 Increased Surveillance of Overseas Transactions

The need to strengthen monitoring of tax avoidance has been raised due to the diversification of asset management and internationalization of the wealthy. In particular,

the surveillance enhancement sector is overseas transactions. There is an increasing number of cases of hiding income by using foreign corporations. For example, the owner of a company is avoiding surveillance by moving funds to three foreign countries using ghost companies. However, since 2017, the National Tax Service has introduced a common reporting standard (CRS) so that international financial account information can be automatically exchanged, providing information such as income. The National Tax Service uses various information such as CRS information and overseas remittance to focus on a clear grasp of overseas transactions and overseas asset-related income. It is becoming increasingly difficult to avoid taxation by moving funds abroad.

5.3 Increased Monitoring of Inheritance Tax

The taxation network of the wealthy is also affecting the inheritance sector. The Japanese government will strengthen the prevention of inheritance avoidance using tower apartments by establishing an expert meeting on apartment-related property evaluation standards in 2023.

6. Conclusion

The Japanese wealthy play a role in driving the flow of funds, and they lead the domestic flow of funds. When funds are collected in the market through this, ordinary investors also join and overheat occurs. However, not all asset growth succeeds. Sometimes they fail greatly. When their assets decrease, they respond in a variety of ways to manage their assets. One of them is the tax saving method. The first is the method of using depreciation. In companies, depreciation is generally applied to facilities, but the Japanese wealthy avoid taxation by damaging the years of use and the upper limit regulation. Second, it is a method of using a refund for violation of life insurance cancellation. It is divided below the upper limit regulation amount. For example, if the refund for violation of the cancellation exceeds 1 million yen, the life insurance company is obligated to provide the details of the refund to

the tax office. However, if paid in installments, the life insurance company is not obligated to provide, and the recipient is not obligated to pay income tax. Third, it is the establishment of a public interest foundation and fund. The establishment of a public interest foundation and fund has the effect of reducing taxable income through donations. On the other hand, it is also possible to serve as a shareholder of related companies at the same time, which is also used as an expedient for the succession of the founder's family. In particular, establishing a fund is relatively simple, and the amount and operation are simple, so it is a preferred method. Fourth, the hometown tax system is popular in Japan recently. The hometown tax system is a tax law created for the purpose of bridging the gap in large cities, responding to tax reduction due to the reduction of the urban population, and local development. The hometown tax payment receives tax benefits such as taxation on the donation amount and resident tax. It is an attractive method as a tax-saving method for the wealthy. It is one of the preferred systems for the wealthy because it is possible to donate to the local area, tax benefits, and use of local accommodation and tourism leisure is also available. In recent years, the use of the hometown tax system in Japan is on the rise and is expected to increase further in the future. Fifth, it is a method of overseas immigration. Acquiring an overseas permanent residence is not subject to inheritance tax. Therefore, the number of wealthy people prefer overseas immigration to avoid inheritance tax is increasing.

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