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Fight against Tax Evasion

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- I. Overview**
 - II. Field Audit**
 - III. Penalty**
 - IV. Special Audit by Regional Taxation Bureau**
 - V. Criminal Investigation**



I. Overview

NTA as audit oriented tax administration

- More than 65% of the staff are involved in field audit
- Total numbers of audit . . . 312,000 (FY2003)
- Additional tax revenue . . . ¥ 493billion
- Coverage ratio . . . 3.9%(Corporation)

Supporting systems for audit-based compliance measures

- **Database system**
(KSK online computer network)
 - **Backstopping from regional taxation bureaus**
(information, guidance and manuals etc. . .)
 - **Special Audit**
 - **Large enterprise audit**
 - **Criminal investigation**
- Conducted by
Regional Taxation
Bureaus**

Audit by Regional Taxation Bureaus

- Large enterprise audit
 - About 37,000 enterprises (1.3% of all Co.)
 - About ¥6 trillion corporation tax paid (65% of total revenue in corporation tax category)
 - About 2,200 staff
 - About 4,400 examinations per year

Large enterprise

- Domestic Co. with capital to ¥100 million or more
- All foreign Co. etc.

Audit by Regional Taxation Bureaus

- **Special audit for evasive and difficult cases**
 - About 720 staff
 - About 1,300 cases per year

Difficult cases

beyond the Tax office's investigation resources due to their complexity, difficulty, geographical dispersion, and involvement of multiple tax items

Additional Tax

- **10% or 15% for deficient returns**
- **15% for no returns or a return filed after the due date**
- **35% or 40% for in the case of fraud**

Criminal investigation against serious tax evasion

- **Up to 5 years of imprisonment**
- **About 1,300 investigators**
at regional taxation bureaus
- **About 200 compulsory investigations implemented each year**
- **Close collaboration with public prosecutor's offices**

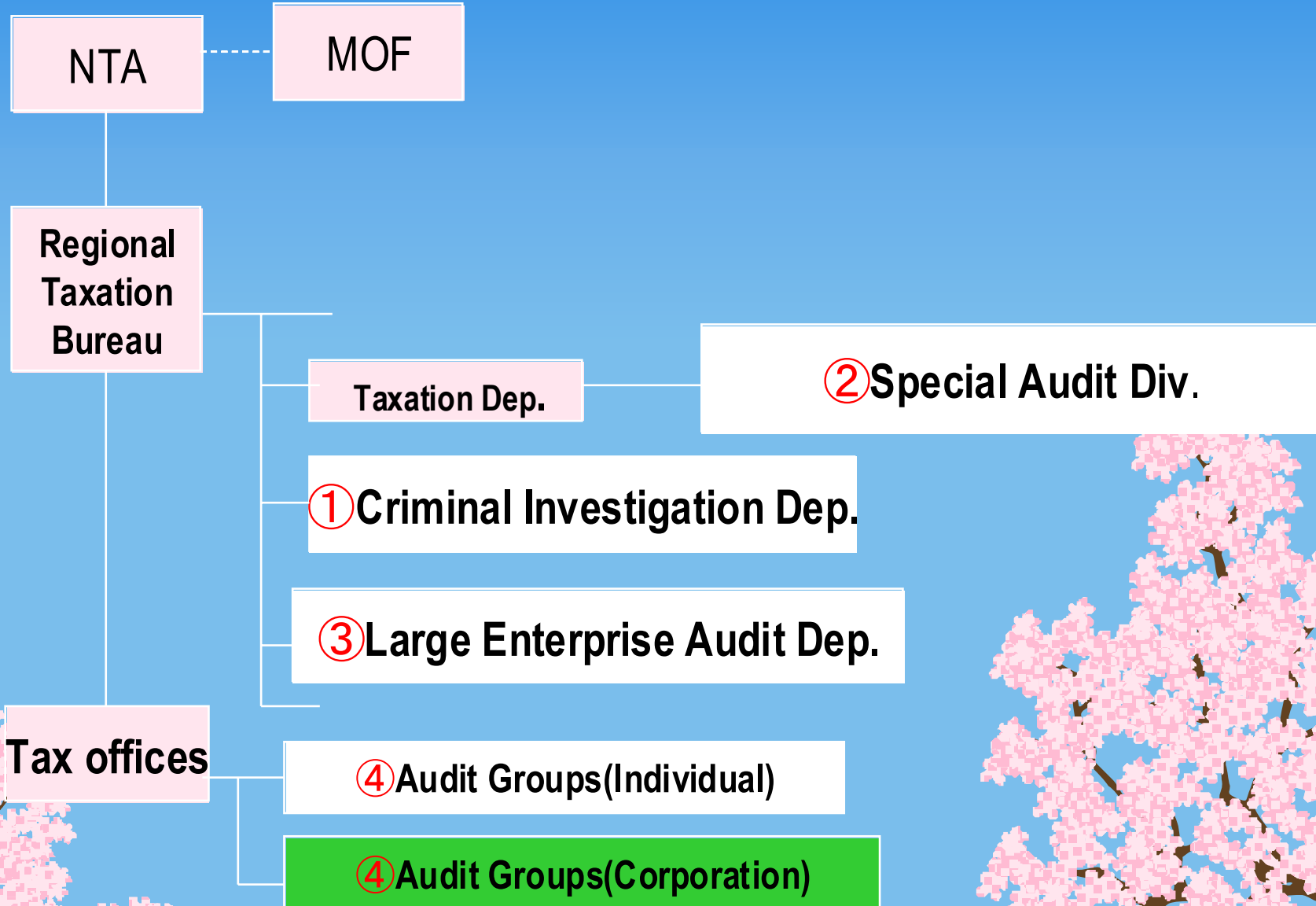
A map of Asia with the country of Japan highlighted in a bright red color. The rest of the map is in a light beige tone. The text "II. Field Audit" is overlaid on the map, centered over the Japanese archipelago.

II. Field Audit

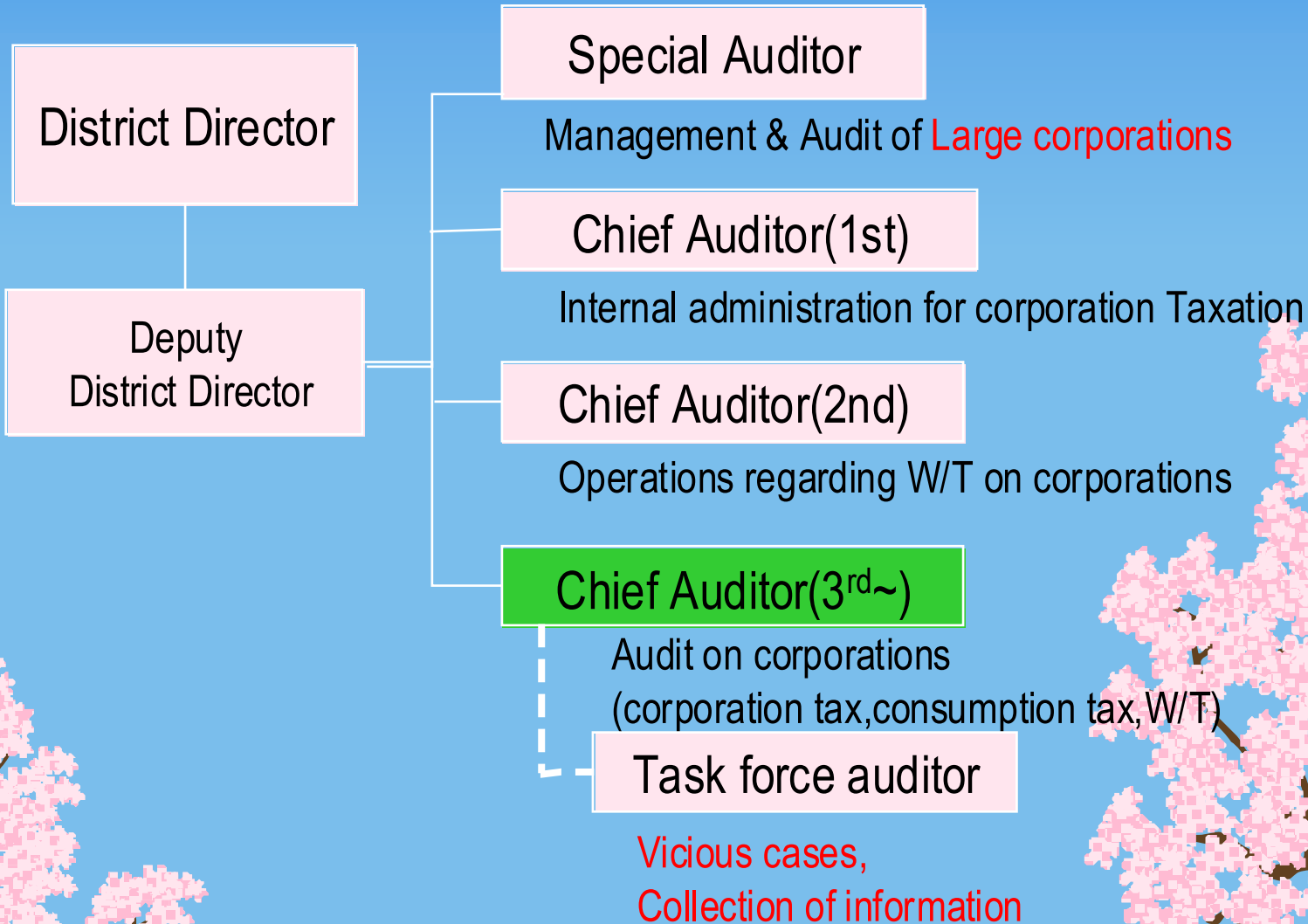
System and Organization to Audit 1

Degree of Difficulty	Procedure (purpose)	Scale of Taxpayer	Department
Large, Pernicious Tax Evasion	Compulsory Investigation (to collect evidence for public prosecution)	ALL	Criminal investigation Dep. of RTB ①
Large, Complicated Cases	General Audit (to examine taxable income of taxpayer)	Small corp. & Individ	Special Audit Div. of RTB ②
General Cases		Large corp.	Large Enterprise Audit Dep. of RTB ③
		Small	Tax Office ④

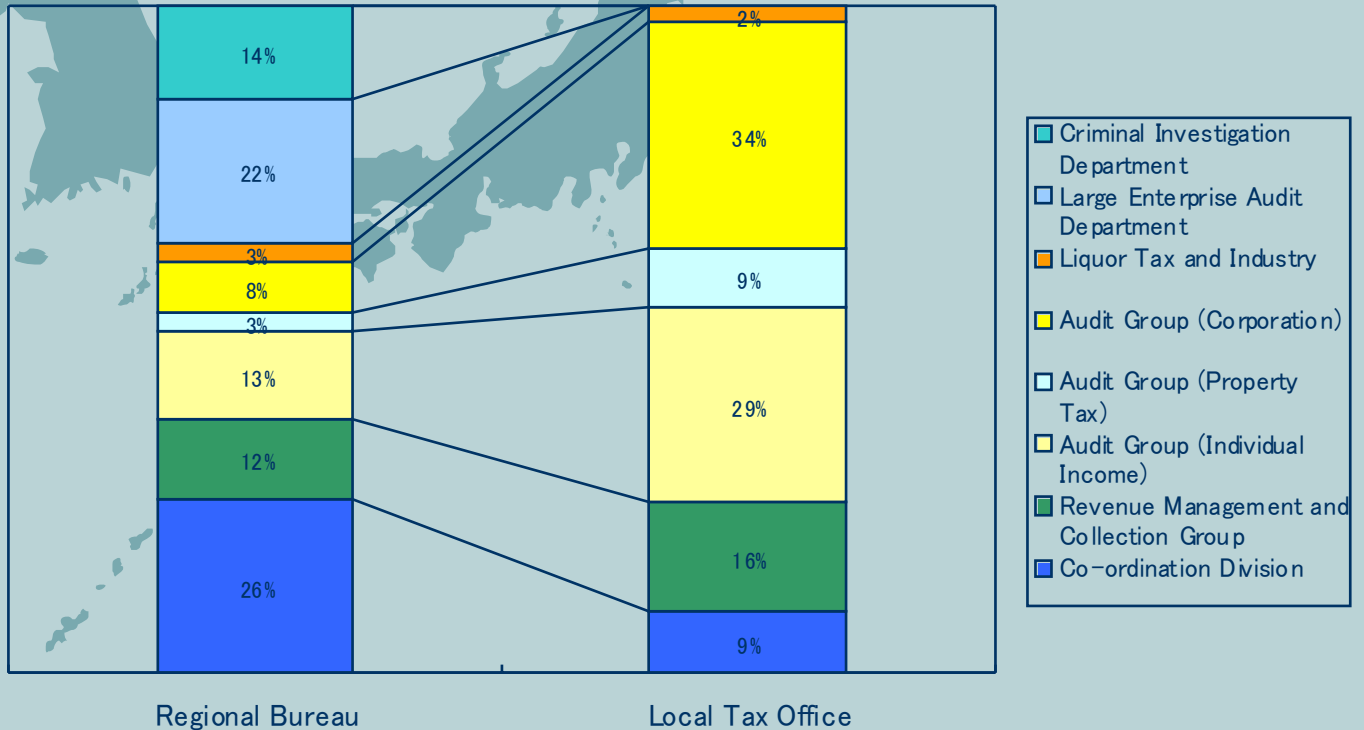
System and organization to audit 2



Organization of **corporation taxation group** at Tax Office



Breakdown of the NTA Workforce



Legal basis of audit

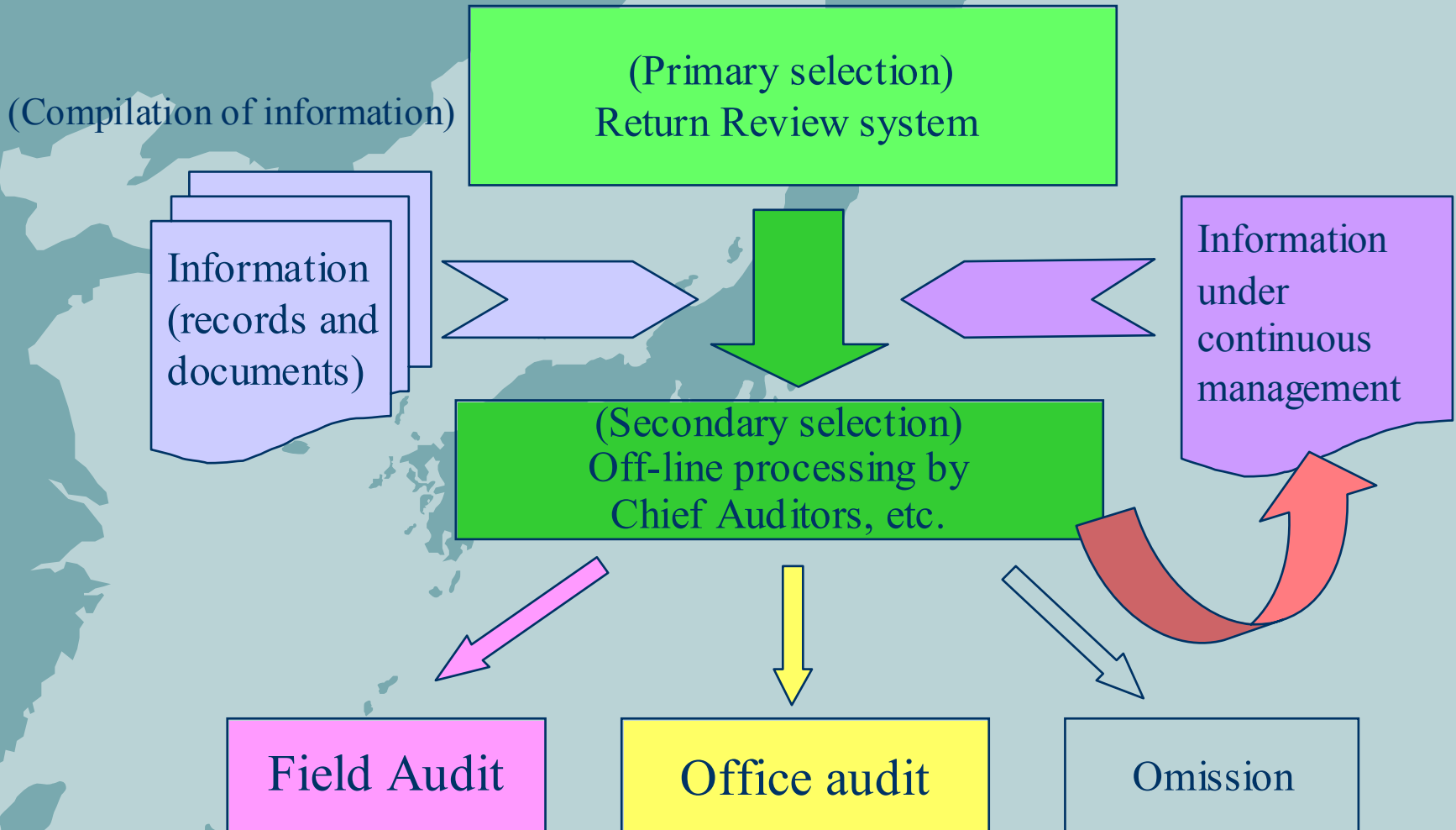
- Authority of Inquiry and inspection
- Penalties for refusing audit
- Confidentiality Obligation

Management of Corporation Taxpayers

- Classification of Corporations
 - Level of Tax Compliance
 - Scale
 - Type of Business

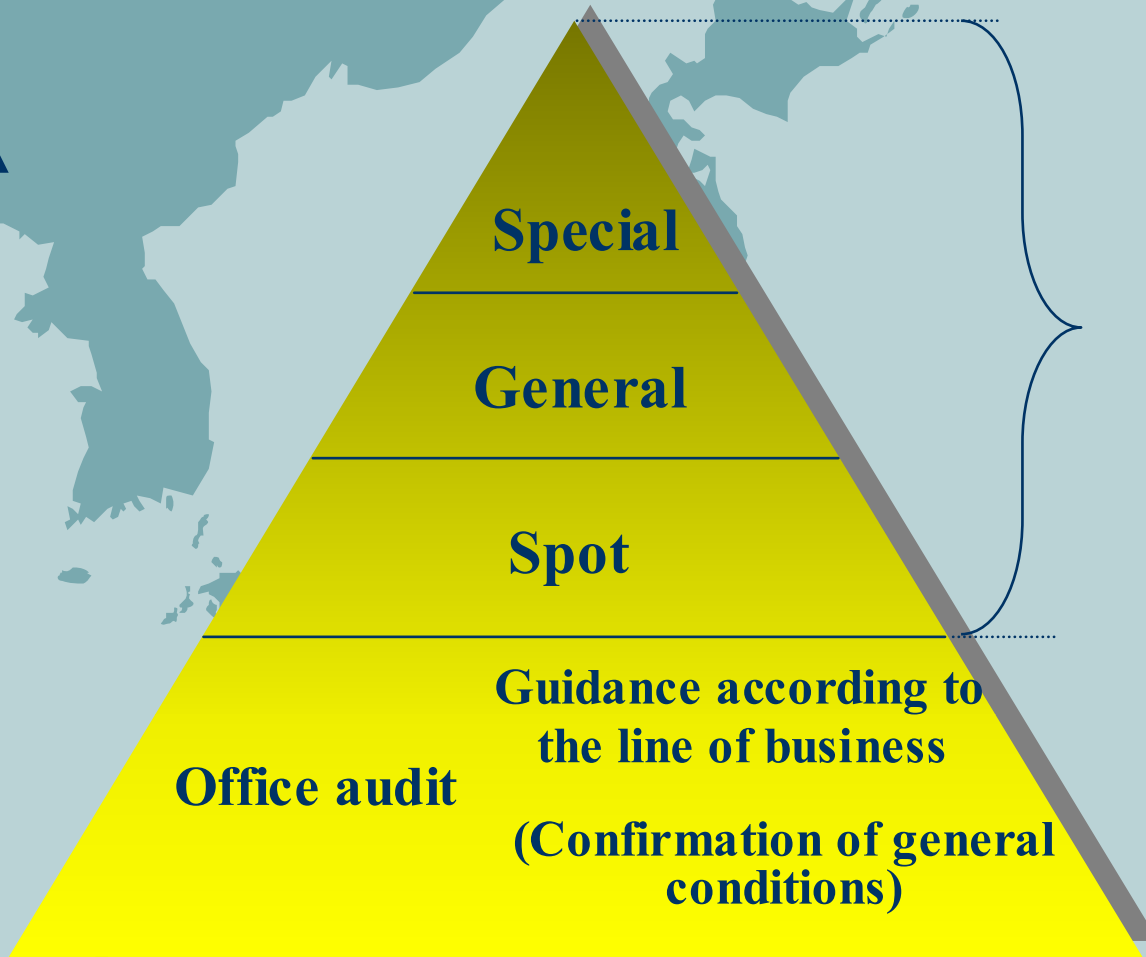
⇒ preliminary selection

(Review of returns)



(System of audit)

Larger amounts, more
malicious or harder
to examine



**Field
Audit**

STEP 1 (Audit)

■ Clerical work (in audit groups)

Storage of documents

- ① Corporation file
- ② Corporation performance file (historical card)

Data management (KSK)

- Input the data of return and financial statement
- Output information which other auditors collected

- Clerical work (in examination group)
 - Input the data (KSK)

return and financial statement

P/L, B/S & attachment →

- sales amounts, cost of sales, gross profit, expenses (reward for representative, salaries, entertainments, etc.)
- assets and debts (balance of borrowed money from representative and others)

STEP 2 (Audit)

- Selection of Suspicious Corporation
 - Analysis by KSK
 - **Business sector**
 - **Compare in the same business**
 - **Fluctuation of Profit rate etc.**
 - **Review of Returns and Records (depend on the experience, at all)**

STEP 3 (Audit)

- **Preparatory Examination**
 - **Analysis of B/S & P/L**
 - **Summary Statement of Business**
 - **Last audit**
 - **Collected Information**
 - **Others**

STEP 4 (Audit)

Notification of audit

- for general field audit
- Usually : 1 or 2 weeks before
by phone
- **without notification**

STEP 5 (Audit)

■ Field Audit

“Mobility“ of auditor is essential

- Books & Accounting Records
- On-site physical examination
- Current state examination
- Supplementary examination
- **Third Parties & Banks**
- Taxation by estimated income

Examination on banks

- **The necessity of Auditing on Banks**
 - Cross reference (need to check the evidence of payment)
- **Why we can Audit on Banks?**
 - - Authority of inquiry and inspection
 - - Agreement (in 1962)
 - - Limitation (whom we can audit)

STEP 6 (Audit)

- Post Audit

Full Explanation of Result

Amendment Return submitted by Taxpayer
or

Correction (Determination) by Tax Office
or RTB

Appellate steps

The characteristics of Japanese Audit

- Mobility (counterpart audit. Bank audit.)
- Information → Management & Selection
- Chief audit system
- On the job training
- Quality and moral of audits



III. Penalty



Penalty for Tax Evasion

- **General Audit**
... **Administrative Punishment**
- **Criminal Investigation**
... **Criminal Punishment**

Administrative Punishment

- **By the General Law of National Taxes, 5 to 40% of taxation amount which has declared incorrectly is added.**
- **Especially when the tax evasion is for the reason of concealment or disguise, heavy additional tax (35 or 40%) is imposed.**
- **Enforced by the Director of Taxation Office based on the general tax audits.**

Criminal Punishment 1

- **Tax laws define the criminal punishment against tax evaders.**
- **Ex. Article 238 of the Income Tax Law**
"where tax evasion has been committed by fraudulent acts, the offenders shall be condemned to prison terms of five years or less or a fine the amounts of which is equivalent to the tax amount evaded, or a combination of the two classes of punishments".

Criminal Punishment 2

- **Imposed especially to the large-scale, vicious tax evaders.**
- **Accused by the investigator to the prosecutor based on the criminal investigations.**
- **Administrative punishment could be imposed on the case of criminal investigation.**

Penalty for tax evasion

Segment		Description
Administrative punishment	additional tax for deficient returns	10% (or 15% for excess of certain amount)
	Additional tax for no return	15 %
	heavy additional tax	35 for deficient returns or 40% for no return
Criminal punishment	Fallacy and other acts of dishonesty	<p>1. 5 years imprisonment or less and/or a fine of 5 million yen, or a combination of two class of punishment.</p> <p>2. Government can impose tax evaders in excess of above mentioned fine if their tax evasion is more than 5 million yen.</p>



IV. Special Audit by Regional Taxation Bureau

Special Examination Team

Special Audit Division
Taxation Department, Regional Taxation Bureau

Information and
Taxation Division

- Large, complicated and difficult cases
- Cases involving multiple tax items or geographically dispersed entities
- Well-known cases and cases involving famous people

Professional Team for
E-commerce Taxation

- E-commerce cases
- Development of information source

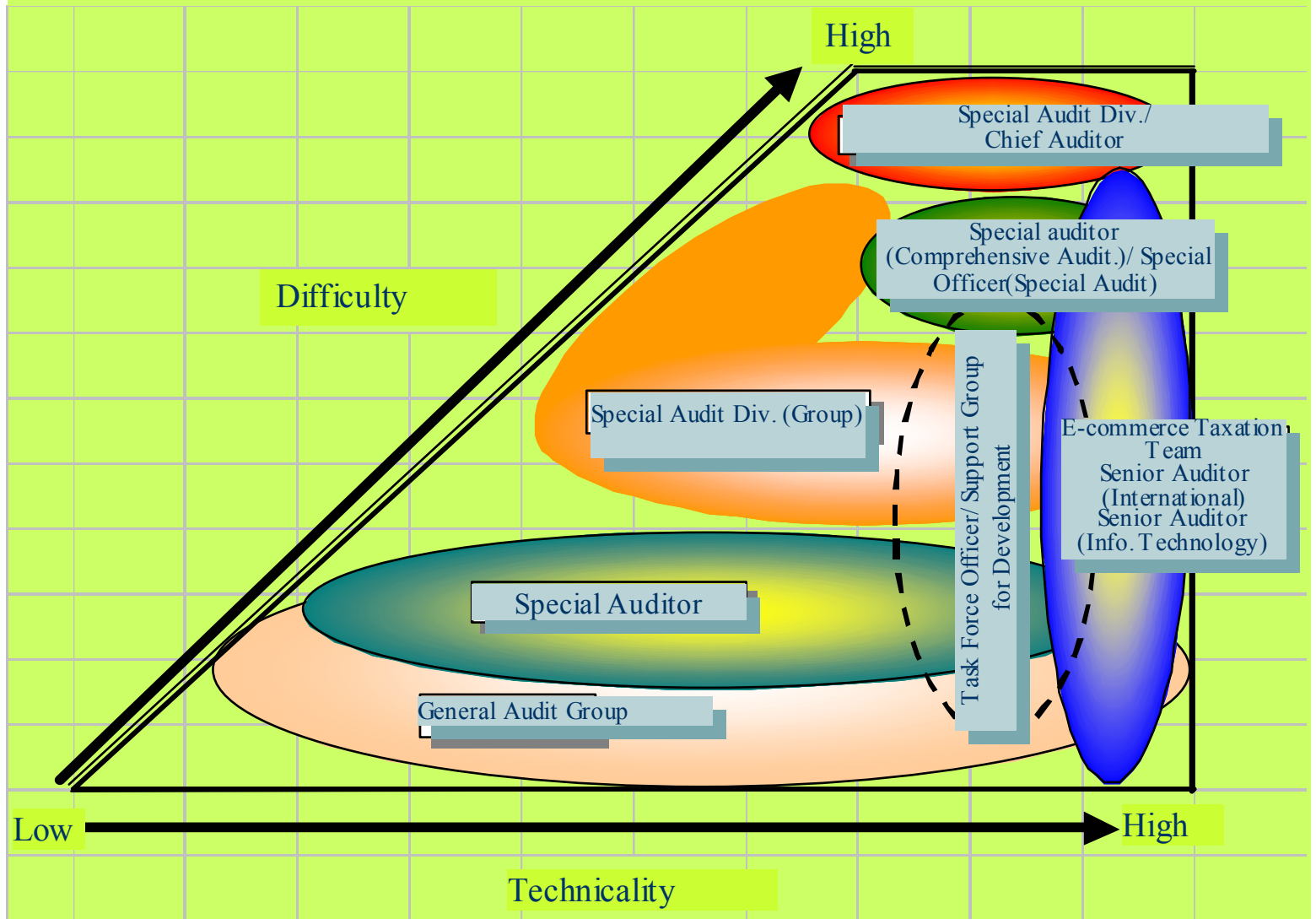
Project Team for
International Taxation

- International taxation cases
- Cases involving international tax avoidance schemes

Creating an Audit Structure for Complex Schemes

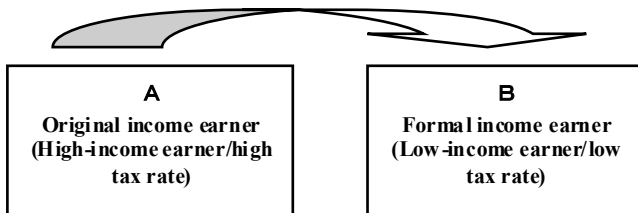
1. Weaknesses of the conventional vertical audit structure
 - ▪ Audit by tax items
 - ▪ Separate audits by regional taxation bureau and local tax office
 - ▪ Separate audits by taxation department and examination department
 - ▪ Disparate management of taxpayers' historical data
 -
2. Project team to address international tax evasion was established in the taxation department of major regional taxation bureaus.
 - ▪ Concentration of international taxation experts
 - ▪ Management of information by business group and family relationship
 - ▪ Thorough simultaneous audits of individuals and corporations in a business group
 - ▪ Collection and analysis of scheme information, and providing them to onsite auditors
 -

(Arrangement map of audit cases)



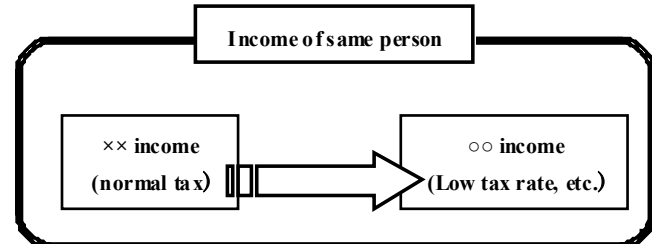
Examples to reduce taxes

Conversion of real obtainer of income



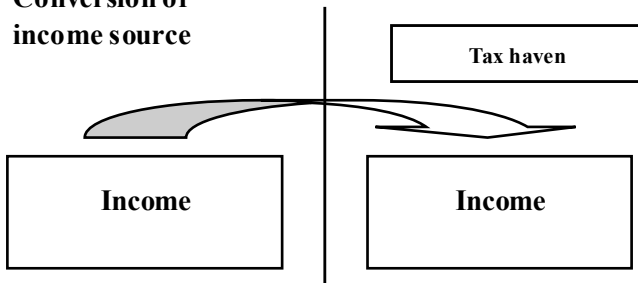
Convert the income belonged to A into nontaxable B

Conversion of income schedule



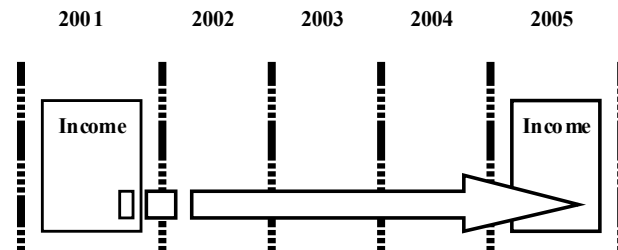
Convert into income with low tax rate, etc., in case the tax rate is different by income schedule

Conversion of income source



Convert the income source belonged to taxable country into tax haven

Manipulation of imputed year of income



Arbitrary manipulation of taxable year

Example 1 : Comprehensive Audit for Corporate Group or Family Business Group

Individual Income Tax

Consumption Tax

Withholding Tax

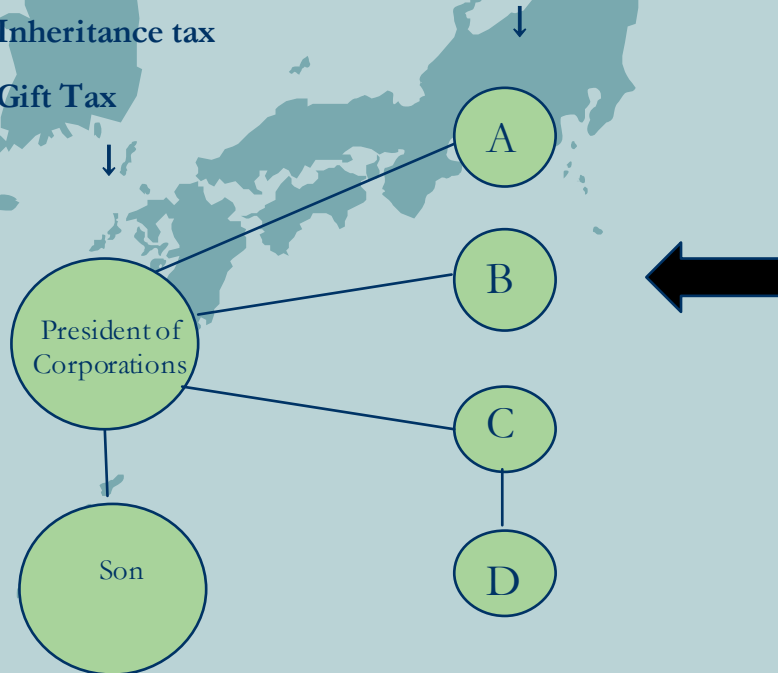
Inheritance tax

Gift Tax

Corporate Income Tax

Consumption Tax

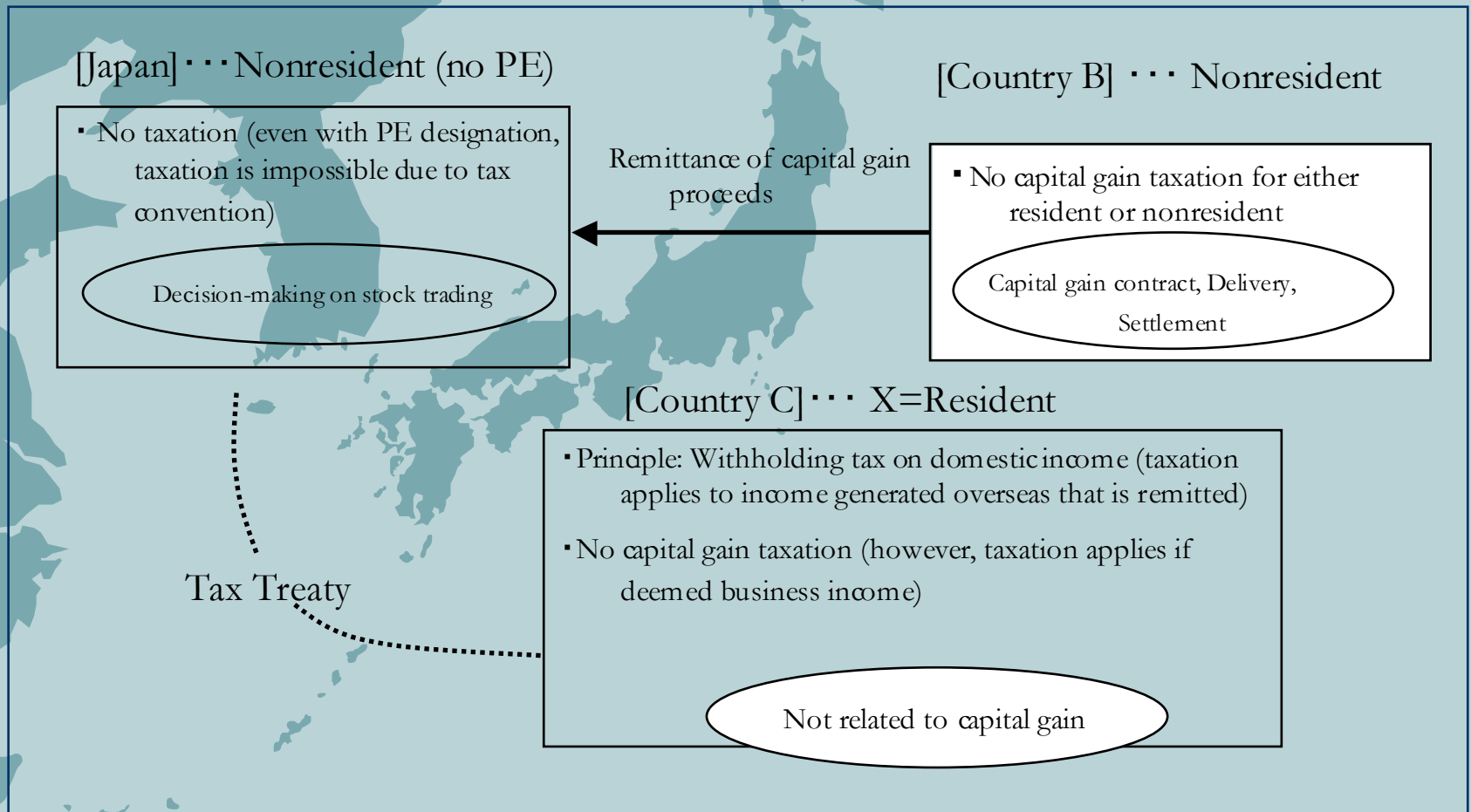
Withholding Tax



Comprehensive Audit

● Example 2: International tax avoidance

—Tax avoidance using nonresident status





V. Criminal Investigation



1. Overview

(1) Role of Criminal Investigation

- **Criminal investigation is the program to investigate the large-scale and fraudulent tax evaders, and charge them to the prosecutors.**
- **Through its “punishing one criminal to take warning of many” effect, this program is for improving compliance, the moral of tax-payment.**
- **“The last resort” of the self-assessment taxation system.**

(2) Organization

- **1,300 Investigators (58,000 officers in NTA, Regional Tax Bureaus, Taxation Offices)**
- **The CID head office of NTA**
- **CID in 11 Regional Tax Bureaus and Okinawa Regional Taxation Offices**

(3) Scope of Criminal Investigation

- **Information gathering from the grasp of the clue to the commencement of investigation**
- **Duties from the commencement of investigation to the accusation**

(4) Judgments Handed Down in Criminal Investigation Cases

- Number of Judgments 133
- Number of Convictions 133
 - Number of Convictions with Prison Sentence without Probation 6
- Amount of Tax Evaded per Case
\155million
- Average Prison Sentence per Person 15.6monts
- Average Fine per Case \32million



3. Procedure

(1) Procedures from Investigation to Verdict



(2) Collection of Information

- **During the past 54 years since the criminal investigations system was started, there have been a total of more than 13,000 cases of investigations conducted.**
- **There have been a diversity of motives behind the initiation of these investigations.**
- **The most important thing is how to pick up the large-scale, vicious tax evaders.**

<Basic Data>

- **Investigations of business conditions on the industry-by-industry basis and the establishment of business and the opening of stores and shops.**
- **Competitive studies of business performances of taxpayers in booming industry, performance comparison with a same trade.**
- **Data in KSK (NTA comprehensive information management system).**



<Information from the Public>

➤ Lots of information is provided from ordinary people to the Regional Taxation Bureaus or Tax Offices.

...Some of concrete and assured tax evasion related information is included.



<Information from the Media>

- Articles about types of business currently in boom**
- Advertisements sensationally displayed in a variety of magazines**
- Articles about luxurious lives of people**



<Primary Investigation>

- **After examining of basic investigation results, the primary investigation will be initiated about relevant taxpayers when the huge tax evasion would be expected.**



(3) Meeting for Open Investigation (the compulsory investigation)

- **When the decisive evidence of tax evasion is obtained through the primary investigation, meeting to determine whether the open investigation (the compulsory investigation) should be initiated is held.**



(4) Preparation for Open Investigation

- **Claim for court permission to conduct the compulsory investigation.**



(5) The Initiation of Open Investigation

- **Entries of special agents, carrying a warrant issued by a judge, into the houses and offices of suspects as well as the offices of their business connections to make through, simultaneous searches.**
- **Seizure of books and other material evidence necessary to prove the facts of tax evasions.**



(6) Mobilization of Special Agents

- **In the Regional Taxation Bureaus with larger areas, roughly 40-60 places are searched and about 150-180 special agents are mobilized for a case of tax evasion.**
- **Mostly, the investigation starts all at once around 8 a.m.**



(7) Accusation Procedures 1

- **When the conclusion at the meeting is to prosecute the case, procedures for the prosecution are immediately taken.**
- **The document and the evidence will be translated to the prosecutors.**
- **The case will be in hand of the prosecutors.**

(8) Accusation Procedures 2

- **The prosecutors will carry out their own investigations on the accused case in accordance with the Code of Criminal Procedure.**
- **Indictment at a court ⇒ Court judgment**



4. Statistics

(1) Summary of Investigation

(Unit: Case, %, \million)

	2000	2001	2002	2003	2004
No. of Cases Handled	218	202	195	201	210
No. of Cases Disposed	205	212	196	202	213
No. of Cases Accused	146	151	145	147	152
Accusation Ratio %	71	71	74	73	71
Tax Evasion Amount	27,088	31,942	35,683	33,613	28,224
Tax Evasion Amount per Case	132	146	182	166	133

(2) Businesses with Heavy Accused Caseload

2002		2003		2004 (Unit: Case)	
Category of Business	Cases	Category of Business	Cases	Category of Business	Cases
Construction	10	Machinery Retail Sale	10	Food & Beverage Retail Sale	11
Real Estate	8	Software	7	Machinery Retail Sale	8
Entertainment	6	Construction	7	Pachinko parlor	8
Food Manufacturing	5	Money Lender	7	Medical Service	8
Carriage	5	Cabaret & Restaurant	6	Cabaret & Restaurant	7
Cabaret & Restaurant	5	Real Estate	5	Construction	5
		Pachinko parlor	5		
		Entertainment	5		

(3) Summary of Judgment in First Trial

Year	Judgt. case	Guilty case	Penal service guilty	Guilty %	Tax per case	Punishment per person (Months served)	Liability per person or corp.
			(persons)	(%)	(million yen)	(months)	(million yen)
2002	170	170	4	100	93	16.0	23
2003	133	133	6	100	119	13.6	26
2004	171	171	11	100	111	15.3	27



Thank You