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Notes

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Abstract

Considering not only the basic income tax treatment but also the recent cases, this note discloses some specific tax problems in Japan and the necessity to update the rules of the income tax law. An analysis of leading cases in this area also suggests its importance. The purpose of this note is to introduce specific issues in Japanese income tax law and to investigate how we can improve the income tax system by comprehensive study from basic rules to the recent cases.

To begin with, Part I overviews the treatments of business expenses to show the issues with some leading cases under the Individual Income Tax Law. Part II introduces and analyses the recent cases and then concludes with my suggestions as to how to improve the tax rules in Japan.

Keywords: Individual income tax, income classification, necessary expenses, business income, personal expense.

Introduction

This note focuses on recent tax cases about the deductibility of expenses under the Individual Income Tax Law (“the IITL”) in Japan. Not only comprehensive research about the treatments of expense under IITL but also analysis of the recent case around expenses treatments show the necessity to update the rules of income tax law. Consideration of historical leading cases in this area also suggests its importance. The purpose of this note is to

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investigate how we can improve the income tax system by comprehensive study from basic rules to recent cases.

To begin with, Part I gives the overview of the Japanese individual income tax system and the general treatments of expenses with some analysis of the historical leading cases under IITL. The part II researches and analyses the recent cases and then concludes the results. This note does not deal with tax timing¹, corporate taxation, or international taxation².

I General Rules

1. Overview

The amount of individual income tax is determined under the rules of the IITL³. The deductions of expenses constitute part of its determination. Deductions come in two varieties: deductions for income and deductions from income⁴.

First, deductions for income are typically business expenses, which are generally spent for getting profit and subtracted from gross receipts to determine total ordinary income. Additionally, the cost to acquire an asset also comes in this category. With regard to the former deductions, a principle controversy is whether outlays are used for a business or personal purpose. Moreover, how to treat mixed personal and business expenses like commuting to work cost and business meals during work is questionable (and considered below).

Second, deductions from income are certain personal expenses, which are listed under IITL and are partly deducted from total ordinary income to reach taxable income. There are 15 kinds of deductions listed, such as basic deduction for the taxpayer himself, medical expense deduction, certain insurance expenses, and charitable contribution deduction⁵. Those deductions are the chief exceptions to the tax policy that personal expenses are disallowed⁶. The technical problem in this area is regressiveness because of lack of a phasing-out rule for high-income taxpayers.

This note chiefly considers the deductions for income. Those are subtracted from gross receipts to determine total ordinary income.

“Gross receipts” mean all wealth gained by an individual in a taxable

year, including rights to get wealth under a comprehensive income concept⁷. However, there are exemptions listed under Article 9, which are originally excluded from gross receipts⁸. Gross receipts are classified into 10 categories of income depending on their sources under the IITL: interest income, dividend income, real estate income, business income, employment income, retirement income, timber income, occasional income, capital gain, and miscellaneous income. By adding these up⁹, the total ordinary income is determined. And then after applying a single progressive rate schedule to such ordinary income¹⁰, the taxpayer may use some tax credits to arrive at the final amount due.

It is assumed that the classification of gross receipts makes it possible to differentiate the way to calculate the amount of taxable income in accordance with the taxpayer's ability to bear the costs of government, tax burden as well as the way to levy tax due to administrative convenience¹¹. Normally, the treatments of business income and real estate income are pretty similar to ones of corporate income. However, treatments of incomes particular to individuals are different from them. For example, it is deemed that the compensation which an employee receives on her or his retirement has less ability to bear tax because it is likely to support the taxpayer for the rest of her or his life. Thus, the IITL provides a special tax break for retirement income by separately applying the tax rate¹². As another example, a taxpayer receiving gross receipts put in the category of "temporary income" is allowed to deduct directly-matching expense and special amount (¥500,000) from his gross receipts, and then only half of the remaining amount of it is taxable, because gross receipts in the category is viewed as a sort of windfall, like a lost money or property, money won by gambling, a gift from a corporation and so on and those are assumed to have less ability to bear tax. At last, the temporary income add to the total ordinary income.

As described above, each classification has a distinct calculus and treatments. One's tax burden depends on in which category the gross receipts is placed. It sometimes triggers acute conflicts between the National Tax Agency (the NTA) and taxpayers¹³. To illustrate such conflicts, let me briefly introduce one famous and informative case.

Stock Option Case¹⁴: A taxpayer (X), a corporate executive, was granted an option by his employer's parent company (P) to purchase 50,000 shares of

P for ¥1,000 a share. The option was exercisable at any time within the next 10 years, but it was not transferable to others and could only be exercised if X was then still an employee of the company for 6 months after the issue date. Later, X exercised the option. By that time, the market value of the P stock has risen, so that by exercising the option X acquired property value of ¥410 million for cash investment of only ¥50 million. Plainly, X has made an economic profit of ¥360 million--the gap between ¥410 million and ¥50 million. The question that arises was whether that economic profit was classified as employment income or temporary income. Of course, in this case, X filed it as temporary income to enjoy the tax preference: half taxation. As opposed to this, the NTA (Y) regarded the economic profit as employment income. Employment income is calculated, like this: Gross receipts – the estimated expenses fixed by the IITL¹⁵.

Stock options are typical incentive compensation for employees, based on the idea that hard work for the company directly or indirectly may well result in the rise of stock value. The difficulty of this case is that X obtained not his company's stock options but his parent company's stock options and later the real P's stock. In regard to this point, the Supreme Court took it into account that the shares of X's company were held 100% by P and totally under P's control. Accordingly, the main issue to be considered here is whether this income is employment income or temporary income.

The district court held for X on the ground that the gross receipts were generated because of his luck in the stock market, but the court of appeal and the Supreme Court held for Y. The Supreme Court pointed out that since the company adopted the stock option for incentive to obtain employees' diligence and X was able to gain the stock option on the condition of his labor, the economic profit clearly had the nature of compensation. But for X's status as an executive in his company, he would not get such profit, thus the judgment of the Supreme Court is reasonable¹⁶.

Yet still, we should not overlook the background of this case that under the former income tax circular the NTA used to treat the economic profit by execution of stock options as temporary income¹⁷. But later suddenly it changed and treated the profit as employment income¹⁸, since stock options have been adopted among the number of companies. Moreover, Article 84 in the Constitution of Japan states that no new tax shall be imposed

or existing ones modified except by law or under such conditions as law prescribe. In consequence, it is a problem that the NTA changed the way to tax without any revision of the former law¹⁹. Additionally, the assessment by the NTA was doubtfully against the principle of good faith. Such a disorder probably reflected the fact that the income classification could not deal with unanticipated profits in a new situation.

Some argues the final decision meant that full amount of the economical profit should be taxable putting aside a problem of income classification and this case raised the question if our system practically needs the classification of temporary income²⁰.

2. Deductions for income: Expense

As to expenses, whether an expense is deductible²¹, the extent of deductible expense and special deductions are different from each other. For example, under the determination of the amount of employment income, a taxpayer is allowed to deduct only the estimated expense fixed by the statute without any choice²². On the other hand, a taxpayer who runs a business is allowed to deduct the actual amount of expense which he spent for his business²³. Business income is characterized as the mixed income of asset and labor and sometimes the extent of business income becomes questionable.

Moreover, due to this difference and ambiguity, taxpayers try to put their gross receipts abusively into a favored class of income. Namely, if one notice that the final amount of tax determined as employment income is smaller than one when the receipt is taken as business income, he or she would like to put the gross receipt into employment income classification. To illustrate this problem, I will consider one of the famous cases about income classification.

Business Income v. Employment Income case²⁴: A taxpayer (X), an attorney at law ran his own law firm, became a legal counsel of his clients and received fixed compensations monthly from them. X treated the compensation as employment income. The NTA (Y) argued that this compensation was classified as business income. In this case, if X had filed it as business income, the deductible expense would have been smaller than the estimated deduction for employment income.

Stating that income classification should be decided by the legal character of

each income and facts, the Supreme Court made clear definitions of both incomes: first, business income is income out of a business set up on one's account and risk for pursuit of mercenary profit and showing the objective intent and social position to repeat deals with continuity, and second, employment income is from payments received from one's employer in compensation for her or his labor under the employer's order on the agreement of employment. In addition, the Court stressed that the payment received from an employer must be the compensation for providing continuous labor or service with some spatial and temporal limitation set by the employer.

As a result, Supreme Court held that the income should be classified into the taxpayer's business income because his consulting was performed continuously without any limitation.

The case shows the definition of income classification is sometimes an important issue when it comes to available expenses. I assume that if there were to be no difference the treatment of expense between the income classifications, such a conflict could be avoided. I do not mean a repeal of income classification be recommended. Instead, we need more fundamental discussion about it to preparing for facing unseen situations in the future.

Before looking attentively at the recent cases, I will explain the basic rules of expense in detail. After explaining the basic rules for expenses under the IITL, I will consider how to treat mixed expenses and special treatments.

(1) Business expenses -- "Necessary expense"

Article 37 of the IITL is the most comprehensive of the articles concerning expenses. It allows taxpayers who earn income from their businesses, timbers and miscellaneous incomes to deduct "necessary expenses". For example, necessary expenses from business constitute mainly two kinds of expenses: 1) the cost of goods sold and expense required directly to generate the business income from a business and 2) expenditures in the ordinary course of the business which is incurred within a business year. Based on the matching principle, the first is generally referred as a "direct-matching necessary expense" and the second is "indirect-matching necessary expense".

In contrast, Section 162 of the U.S. Internal Revenue Code (I.R.C.) provides that there shall be allowed as a deduction all "the ordinary and necessary expenses" paid or incurred during the taxable year in carrying on any trade

or business²⁵. Unlike Section 162, Article 37 doesn't have the "ordinary" requisition for the deduction. Thus, under the U.S. law but not Article 37, there is an argument if the deductible expense under the statute needs to be ordinary²⁶.

(2) Personal and Mixed Expenses

For tax purposes, the importance of expense is obvious. Generally, income taxation is supposed to tax annual net increment to assets plus annual consumption. While expenses to gain profit on the course of business should be allowed to deduct as business expenses from its gross receipts, outlays for consumption such as personal, family and living cost must be disallowed. Unfortunately, there is no clear boundary between them, since the expenditure spent by the self-employed for her or his business often has the nature of consumption, too. Therefore, it is not easy to treat such mixed personal and business expenses ("mixed expenses").

Article 45 of the IITL is the main statute which prevents taxpayers from deducting personal expenses. It provides that living costs and a certain part of costs related to living costs are disallowed as deduction from business income²⁷. The rest of the costs related to living is equal to mixed expenses. Since costs related to living have both the nature of living cost and of necessary expense, Article 96 Section 1 under the IITL Regulation ("the IITLR") is authorized to clarify the extent of costs related to living to be deductible: it conditions on that the extent should be determined by establishing that the expenditure is used for the business.

For example, even if there is expenditure for dual purpose facilities, the business part of the expenses is deductible when business and personal uses can be separated by reference to the amounts of time, space, and etc²⁸. Otherwise, mixed expenses are not deductible.

(3) Special Treatments

Since the IITL simply adopts each person as a tax unit, there is a potential for abuse: income dispersion by the self-employed, by transferring some fee like compensation, rent or interests to her or his family members. Article 56 of the IITL is a crucial rule for preventing such dispersion. Under the article, a taxpayer is not allowed to deduct the expense paid to his or her family

members who are in the same household finance and who obey the taxpayer in his or her business. Any expenditure paid by the subordinate member is deductible on the taxpayer's return, and the payment to the member is viewed as not payment to the member, which means the income is exempt from the income of the subordinate member. Thus, the article changes partly the taxable unit from the individual to the family.

On the other hand, Article 57 of the IITL allows the taxpayer who files a blue tax return²⁹ to deduct the appropriate payment to her or his family member for the need to keep the self-employed and the closely-held company in tax-parity. Indeed this article seemingly pulls the teeth from Article 56, but some cases show difficulty on applying the article.

Article 56 was rooted in the old statute set forth over 70 years ago to avoid the income dispersing abuse under the possibility that compensation to family members might be too excessive. Nowadays, a husband and his wife, each can be engaged with a sole-business, say, one could be a lawyer and the other a tax accountant, and the husband paid an appropriate fee to his wife for her professional work. This does not seem to be any abuse intent. However, the courts have held that in such a case, the husband may not deduct the compensation under Article 56³⁰. These decisions have been considerably criticized on the ground that the statute was anachronistic³¹. However, Article 56 still plays an important role against income dispersion and any revision accompanying administrative burdens has not been expected.

This limitation is in the category of taxable unit rather than in the category of expense. So this note will not deal with it any more.

3. Two issues of Expense Deductions

On the whole, there are a couple of real difficulties in the existing individual income tax law; first, necessity of considering to what kind of incomes a certain expenditure is attributable because of the income classifications and second, distinguishing the personal expense and business expense because of variety of consumption by the business owners³². Recently we have the very tax cases related to these two points in Japan.

II Recent Cases

The first case (1) is related to mixed expenses and the second case (2) is to income classification between temporary income and miscellaneous income. Notwithstanding that both are pending in court, they are so interesting and still worth considering now. I will omit the subtle details of the case facts for better understanding.

1. Meal fees in the executive meeting of attorneys at law³³.

(1) Facts

A taxpayer, plaintiff (X) is an attorney at law in Sendai, Japan and worked as a dean of Sendai Bar Association as well as a sub-dean of Japan Federation of Bar Association (“the JFBAs”). He spent his money for social events held by the bar associations and their elective campaigns. He filed his tax return in which he deducted those expenditures as necessary expense from his business income. Later, the NTA (Y) redetermined his income tax for the reason why the expenditures were not necessary expenses. After pertinent tax procedures, X sued for the refund of the increased tax. The main issue was whether the expenditure is deductible from X’s gross receipts of his business as a necessary expense : “indirect-matching necessary expense”.

(2) Courts’ Opinions

The district court in Tokyo denied deductions of those expenditures, though X argued that the expense should be deductible because it contributed to X’s business. The court reasoned that since each member of the JFBAs and the JFBAs themselves were different entities and the fruits of the expenditures were attributable to the JFBAs, X’s activity for the JFBAs was not X’s business and then the expense was not be able to deduct from the gross receipts of X’s business income.

X went to the court of appeal in Tokyo. Reversing the district court in the result, the court of appeal approved the X’s position and allowed some part of the expenses to be deductible as necessary expenses from the gross receipt of X’s business income.

Like the district court, the court of appeal also recognized that since each member of the JFBAs and the JFBAs were different entities and the

fruits of the expenditures were attributable to the JFBAs, X's activity for the JFBAs was not X's business. This would mean that X could not earn income by the activity in the JFBAs. Nevertheless, the court stated that since the operation of the JFBAs are closely connected with X's business and financially supported by the members, the expenditure shall be "indirectly matching necessary expense" to the extent that it was needed for the JFBAs executives' operation. Before stating this, the court made sure that the "direct" requirement should be gotten rid of from the deductibility requirement for "indirectly matching necessary expense" because of lack of any statute that provide such a word literally, even though in practice the NTA has needed direct relationship with the business to allow expense deduction. Thus, the court allowed X to deduct his fee for the social events held by the JFBAs but disallowed the fee for second-parties after the events.

(3) Comments

Meal fee in this case is a typical entertainment expense. Practically entertainment expense is all deductible for individual income tax purpose. Unlike this, corporations' entertainment fee is strictly limited to deduct³⁴. Usually meal fee is one of the most important items which is mixed with personal expenses.

Both courts drew different conclusions regarding the issue, even though they were based on the same premise that X's business and the JFBA's operation were separate. Additionally, both recognized the JFBA's operation is necessary for lawyers who has to be a member of certain district of the JFBA's in order to work as a lawyer in the district of Japan. While the district court accepted most of Y's argument and held for Y, the court of appeal held for X. There are two points to be noted in the latter decision.

First, the court of appeal found that the events' indirect relation to the business after recognizing that deductible mixed expenses do not need to be "directly" related to the business because of lack of any statutes which provide that requirement. This point is noteworthy from the constitutional point of view.

Second, possible mitigation to the ambiguity of mixed expense by the court of appeal is that it drew a definite line between personal expense and business expense: the fee for the social events held by the JFBAs and the fee

for second-parties after the events. According to the court of appeal, the latter events are more personal than the former events. But the standard shown by this decision might make the first event longer and cause second parties' cancellation. This does not always provide a real solution.

Y appealed to the Supreme Court right away. Many tax practitioners are interested about the final result, for it will have a broad influence over tax treatment of professionals' payments for events held by their associations.

One more thing to be considered is how we would treat the expense if X was hired by a corporation and it paid the fee. The part of X's expenditure which was judged as personal fee would be treated as salary to X and the rest also would be the expense for the corporation³⁵.

2. Expense of the betting tickets on horses³⁶

(1) Facts

A salaried worker (X) had spent a lot of money to purchase betting tickets on horse races held by Japan Racing Association ("JRA"). He usually did it though the internet following racing tips provided by computer software (A-PAT). He won about ¥ 3.01 billion for three years whose all tickets cost ¥ 2.87 billion, so the net profit was ¥ 0.14 billion. However, X did not file any profit on his tax returns for those years. Therefore, the NTA accused for his failure to file under Article 241 of the IITL. Then a prosecutor (Y) indicted X for it and tried to find the amount of taxes for X to assess his culpability.

Under the IITL, it is interpreted that when an individual wins money by such tickets and it is over ¥500,000, he has to file it as temporary income on the annual tax return³⁷. On filing the return, the temporary income is calculated like this; gross receipt (the money X won by the winning tickets on one race) - expense which is paid directly to get the gross receipts (¥0.11 billion, the expense X paid for the winning tickets). So his temporary income would be about ¥1.45 billion ((¥3.1 billion - ¥0.11 billion - ¥500,000) × 50%). In this calculation, X would have no chance to deduct any expenses for losing betting slips in horse races.

On the other hand, if it is construed that the gross receipt from winning tickets are classified into miscellaneous income, the income will be calculated like this; the gross receipts - total necessary expense to get the gross receipts. Thus, in this construction, X could deduct all his expenses he spent to get the

ticket from the gross receipts and his miscellaneous income would be about ¥0.14 billion (¥3.1 billion – ¥2.87 billion).

Of course, Y assessed the deficiency for X by the former formula and X argued that his income should be calculated by the latter formula. This point is the very issue of the case.

(2) The court opinion

The Osaka district court held X guilty for failure to file and gave X a 2 month prison sentence suspended for 2 years. It recognized normally gain from such tickets should be treated as temporary income, but by considering X's special situation, it decided regarding the tax computation that X's income was classified as miscellaneous income.

It reasoned that X bought a lot of the tickets constantly and automatically for seeking profit and it was characterized as an asset management beyond his hobby. According to this, X's outlay for all the ticket was viewed as cash investment to be collected by their receipts. In other words, he could add the ticket he lost to the total expense. X's amount of the tax should be determined by the formula: gross receipts – total necessary expenses to get the gross receipts. In effect, the court held for X.

(3) Comments

This case is the first case challenging this kind of income classification and interests public peoples as well as tax practitioners. Usually there is a trend to bring some gross receipt into temporally income because of its special tax preference as just we saw in the stock option case. However, X tried to classify his gross receipts from winning tickets into miscellaneous income because he wanted to deduct all expense he spent for the tickets, as described above.

One of the characters of this case is the huge difference of the taxable incomes depending on the income classification. Simply speaking, if the gross receipts were classified as temporary income, the taxable income would be ¥1.45 billion. On the contrary, it is assumed if the gross receipt was miscellaneous income, the taxable income would be ¥0.14 billion. Once we contemplate his ability to bear tax as well as the way he earned the money, the latter choice is more suitable and this idea also matches the original purpose of income classification. Thus, the court decision is plausible.

When the statute was enacted, lawmakers or the NTA did not imagine that people were going to use internet or computer software to purchase the gambling tickets and could keep and probe precise accounts for the deals. Although Y appealed to the upper court, lawmakers should think out any possible new rules for such gambling receipts. At least, the NTA should think about how they will handle if a taxpayer files his receipt from a winning horse ticket as miscellaneous income and tries to deduct all expense of cash investment to the winning ticket. As the court pointed out, in order to classify the gross receipts from winning tickets into miscellaneous income, the taxpayer must be required to establish that purchasing such tickets is equitable to asset management and be beyond hobby with clear evidence. However, if the outlay is still viewed as consumption in part, it would be disallowed under Section 45 of the IITL.

Summary

This note has explained the basic treatments of expense referring to the leading cases and the recent cases. Again, the income classification should be emphasized as the characteristic of the Japanese income taxation system for individuals. It has a big effect on how much expense is deductible, as one of the recent cases showed a good example. The classification is difficult when one faces new type economic value to be taxable and the way to earn income.

It is also difficult to establish certain standards to distinguish personal and business expense by analysis of the recent case, as discussed above. While it seems this situation is as same as seen in American tax law³⁸, there is formidable number of the U.S. cases and rules about the business and mixed expense to be researched. Thus, this note just scratched the surface of expense deduction study and set the initial stage of the comparative law study in this area. Actually such a research is necessary to develop Japanese tax system in which we have a problem of the paucity of cases.

Under the single progressive tax rate, the amount of expenses to be deducted has a direct effect on the final tax amount. Besides we should keep in mind that one small change may cause a big influence to our budget. Moreover, the National Diet ought to re-focus on the importance of the income tax and recognize the current income tax system needs to be more

progressivity especially when they raise consumption tax rate without any measure to ameliorate its regressiveness, and since the budget deficit has reached an astronomical level, extensive attempts are essential in income taxation area, too.

- 1 This includes the timing of deduction issues as well.
- 2 All taxpayers in this note are resident individuals who have address in Japan or have lived in Japan over 1 year except as otherwise expressly mentioned. About the definition of a resident in Japan, *see* Article 2(1)-3 of the IITL.
- 3 The tax rules are separated for individuals and corporations in Japan. The amount of corporate income tax is determined under the Corporate Income Tax Law.
- 4 This way of explanation is referred to CCH Japan Master Tax Guide(9th ed. 2012).
- 5 *See* Articles 72-84 of the IITL.
- 6 The U.S. Internal Revenue Code also has the similar deductions. *See e.g.*, Section 151 of I.R.C. and Edward E. MaCaffery, *Income Tax Law*, 88 (2012).
- 7 Article 36(2) of the IITL.
- 8 There are 18 items of exemptions under the article. For example, certain amount of commuting expense is exempt from gross receipt. *See* Article 9(1)-5 of the IITL.
- 9 Precisely speaking, ordinary income consists of all incomes other than certain income from stock and real estates, interest income, retirement income and timber income. Those incomes are separately calculated and taxed in a distinct way. *See* Article 21(1)-3 of the IITL and Articles 3, 31, 8-4, 37-10 of the Act on Special Measures Concerning Taxation.
- 10 *See* Article 30 of the IITL.
- 11 *See* Hiroshi Kaneko, *Tax Law* 18th ed., 257 (2013, Koubundo).
- 12 Article 28 of the IITL.
- 13 Once we consider not only this classification but also the limited extent of offsetting one income category against other income category, it will be more important issue. *See* Articles 21(1)-2, 69 of the IITL.
- 14 Supreme Court Decision, 25 Jan., 2005 Civil Supreme Court Decision

- Reports vol. 59, no. 1, p64.
- 15 The estimated expense is from ¥650,000 to ¥2,450,000. *See* Article 28(3) of the IITL.
 - 16 However, the profit itself was generated in the stock market. Then, it is impossible to say that the income has two natures; temporary income and employment income. Not surprisingly, courts did not try to divide one income into two kind of income. *See* Matuyama District Court, 18 Apr., 1991, *Syougetsu* Vol. 37, No. 12, p2005.
 - 17 Income Tax Circular.
 - 18 Income Tax Circular 23-35kyo-6. Under later enactment, taxing any economic profit executed by eligible stock option is deferred until the stock was sold. *See* Article 29-2 of the Act on Special Measures Concerning Taxation.
 - 19 Changing tax rule by the circular was challenged in the past and Court pointed out that the lawful tax assessment could not be illegal even if it was authorized by change of the circular. *See* Supreme Court decision 28 Mar., 1958. Civil Supreme Court Decision Reports vol. 12, no. 4, p624. Most tax researchers argued the need of enacting a new law for new treatment. *See generally*, Hiroshi Kaneko, *Jurist 100 Cases of Constitutional Law*, 424-425 (4th ed., 2000).
 - 20 *See e.g.*, Osamu Tanaka *et. al.*, Case File I about Income Tax, 393 (2006, Zeimukeirikyokai). Takako Sakai, Stock Options, *Jurist Tax Case* 100, 70, 71 (5th ed., 2011).
 - 21 For example, interest income is not allowed to deduct any expense. Its tax is separately withheld from gross receipt. Article 23 of the IITL.
 - 22 Article 28 of the IITL.
 - 23 Article 27 of the IITL. In fact, whether the difference on the extent of deductible expense was the fair treatment under Article 14 in the Constitution of Japan was challenged. The Supreme Court held that Congress had a broad discretion to enact tax laws and the difference of this treatment was not unconstitutional. This was famous referring as Oshima case. *See* Supreme Court, 27 Mar., 1985, Civil Supreme Court Decision Reports vol. 39, no. 2 p247.
 - 24 Supreme Court, 24 Apr., 1981, Civil Supreme Court Decision Reports vol. 35, no. 3 p672.

- 25 *See also* Section 212 of I.R.C.
- 26 There are a formidable number of cases about the definition of ordinary. *See e.g.*, Welch v. Helvering 290 U.S. 111 (1933). Depty v. Dupont, 308 U.S. 488 (1940).
- 27 Article 45 also lists certain items which are not allowed to deduct, such as income tax, administrative penalties, municipal inhabitant tax, and so on.
- 28 *See also* Income Tax Circular 45-1.
- 29 By filing a blue tax return, the taxpayer can enjoy many tax benefits. In order to file a blue tax return as an annual tax return, a taxpayer has to get a permission from the relevant NTA officer. A blue tax return has to be accompanied with some financial document proved by some account books. *See* Articles 143, 166 of the IITL.
- 30 *See e.g.*, Supreme Court decision, 2 Nov., 2004, Hanji No. 1883, p43.
- 31 *See e.g.*, Tanaka *et. al.*, *supra* note 20, 201.
- 32 *See* Hideaki Sato, Standard Income Tax Law 2nd ed, 244(2010, Kobundo).
- 33 Decision by District court of Tokyo, 9 Aug., 2011. Decision by Tokyo Court of Appeal, 19 Sep., 2012.
- 34 Under Article 61(4) of the Act on Special Measures Concerning Taxation, an amount of entertainment, etc. a corporation (which has over ¥100 million of capital contribution) disbursed in each accounting period shall not be included in gross expense in computing taxable income.
- 35 *See* Yoshinobu Shinagawa, Deductibility of Meal Fees in the Executive Meeting of Attorneys at Law, 168 Zeiken 78, 81(2013).
- 36 Decision by District court of Osaka, 23 May, 2013. Since neither court nor prosecutor has an authority to determine the amount of tax, the final determination of the income classification in this case will be held finally in its civil case, not in the criminal case.
- 37 Income Tax Circular 34-1 since 1970.
- 38 Boris I. Bittker & Lawrence Lokken, Federal Taxation of Income, Estates and Gifts, ¶ 20.2.1, (Current through 2013).