

Study on Issues and Policy Proposals for Domestic Fund Vehicles

-Comparison between Singapore VCC and Japanese Investment
Corporations-

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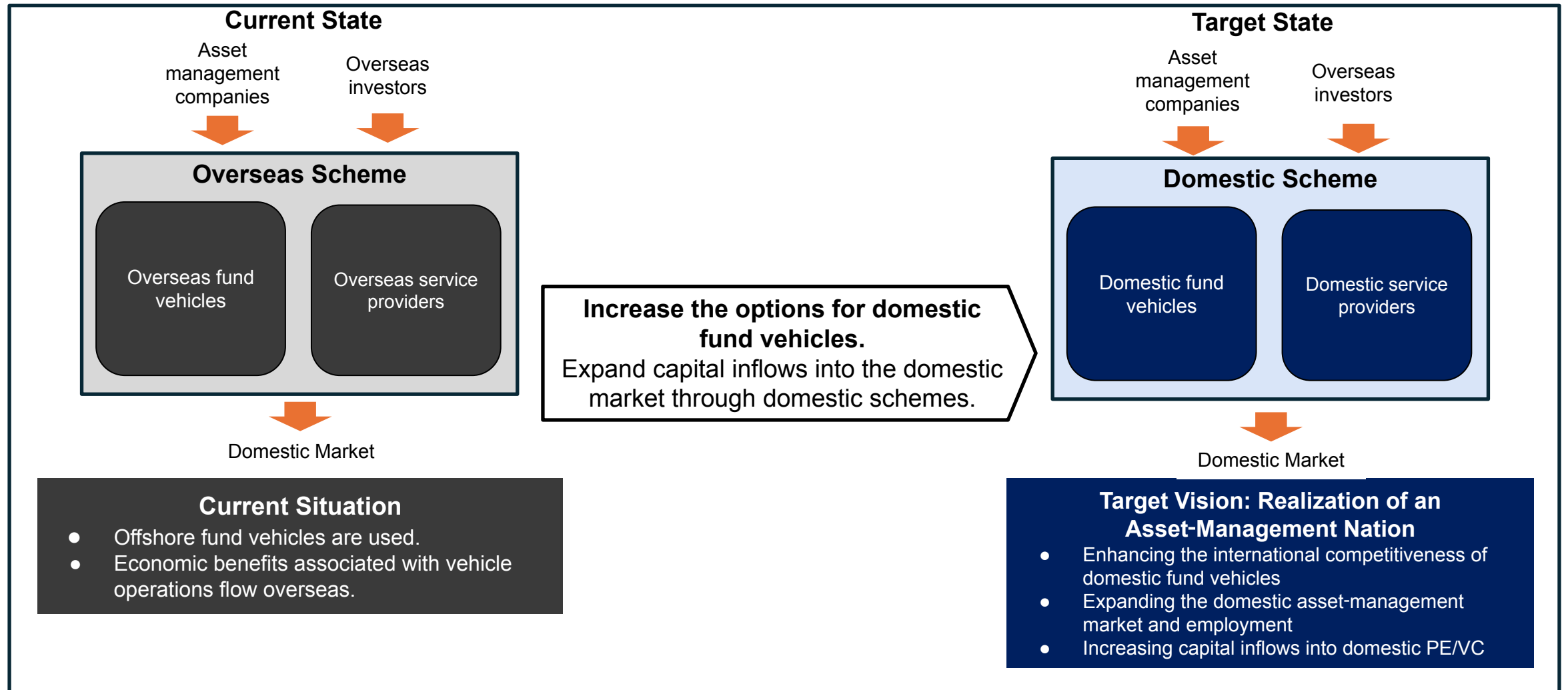
Overview of the Study, Current Situation, and Target Vision

(1) Background and Purpose of the Study

Issues / Problems	Current Understanding	Purpose of This Study
<ul style="list-style-type: none">• Foreign investors tend not to choose Japanese fund vehicles when investing in domestic PE/VC, instead using offshore fund vehicles.• As a result, the economic benefits associated with fund operations flow out of Japan.	<ul style="list-style-type: none">• Issues related to partnership-type vehicles (LPS) were identified in last year's study and partially improved.• Domestic fund vehicles also include trust-type and corporate-type structures, but these have not been sufficiently examined.• As a successful overseas example, Singapore's corporate-type vehicle (VCC) is notable in addition to partnerships.	<ul style="list-style-type: none">• To compare the current state of all domestic fund vehicles (partnership, trust, corporate).• To compare Japanese investment corporations—considered highly applicable to PE/VC—with Singapore's VCC, and derive insights for solving issues in domestic PE/VC fund vehicles.

(2) Current State and Target Vision of the Asset Management Ecosystem

- Foreign investors primarily use offshore fund vehicles when investing in domestic PE/VC.
- As a result, the asset management business ecosystem—including service providers associated with fund vehicles—is flowing out of Japan.
- To realize Japan as an asset-management hub, it is necessary to resolve issues in domestic fund vehicles and make them a viable option chosen by all investors, both domestic and foreign.



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Summary of Findings Issues and Policy Proposals for Investment Corporations

(1) Comparison of Domestic Fund Vehicles

- The partnership-type vehicle (LPS) had its issues identified in last year's study, and certain improvements were made, but issues still remain.
- The trust-type vehicle (investment trust) has long been established as a fund vehicle and is widely used by Japanese retail and institutional investors.
- Its commercial practices—mainly assuming marketable securities as investment targets—are well-established, and changing them is difficult.
- The corporate-type vehicle (investment corporation) could become a viable option; therefore, potential solutions (policy proposals) should be examined to improve usability.

(1) Comparison of Domestic Fund Vehicles

Comparison of Fund Vehicles

Fund Scheme	Partnership Type: LPS	Trust Type: Investment Trust	Corporate Type: Investment Corporation
Main Features	<ul style="list-style-type: none"> Mainly used for PE/VC investment. Not taxed at the fund level (pass-through), avoiding double taxation. Able to value portfolio companies at fair value under IFRS. METI has published a model LPA aligned with global standards. 	<ul style="list-style-type: none"> Long history as a fund vehicle; widely used by Japanese retail and institutional investors. Investment trusts are tax-exempt and avoid double taxation. 	<ul style="list-style-type: none"> General meetings of unitholders and appointment of directors make governance easy to explain. Accounting is completed at the vehicle level, simplifying accounting for investors. Singapore's corporate-type vehicle (VCC) is a successful overseas example.
Current Status / Issues	<p>Issues identified last year are partially solved, but some remain.</p> <ul style="list-style-type: none"> ✓ May be deemed to have a PE and become subject to PE taxation (exemption available via filing). ✓ Pass-through structure makes accounting for partnership gains/losses more complex than other vehicles. <p style="text-align: center;">  Examination of options beyond LPS is necessary. </p>	<p>Practices assume domestic investors and marketable securities; difficult to change.</p> <ul style="list-style-type: none"> ✓ Restrictions on selling to foreign investors by domestic distributors. ✓ Japan-specific accounting and NAV calculation rules. ✓ Additional subscriptions/redemptions generally conducted in JPY (not common in foreign currencies). <p style="text-align: center;">  It is currently difficult to accept foreign investors when investing in domestic PE/VC. </p>	<p>Although investment corporations are used almost exclusively for real estate investment, the question remains why they are not used for PE/VC.</p> <p>Reforming the corporate-type vehicle may be the fastest path to improving the international competitiveness of domestic fund vehicles.</p> <p style="text-align: center;">  Scope of This Study </p>

(2) Comparative Analysis with VCC, Issues of Investment Corporations, and Policy Proposals

- Issues of investment corporations were identified based on a comparison with Singapore's Variable Capital Company (VCC).
- To make investment corporations a more attractive vehicle, the following policy proposals are considered.

Main Differences		VCC	Investment Corporation		Proposed Policy Measures
			Current	Issues	
Accounting	Applicable Accounting Standards	Local GAAP US GAAP IFRS	J-GAAP (Investment Corporation Accounting Rules)	① Significant gap from international standards	① Allow optional application of IFRS
Legal	Issuance of Share Classes	Allowed	Not allowed	② Difficult to approach investors with different needs	② Allow issuance of share classes (multiple unit classes)
Taxation	Tax Regime	Tax Exempt under Sec.13 (subject to conditions)	Pass-through tax regime (not a tax-exempt system) (※)	③ Over-90% dividend distribution requirement To satisfy the conduit requirements, it is necessary to distribute more than 90% of profits as dividends. If the amount of dividends distributed is less than the taxable income, taxation will arise at the fund level.	③ Relax the 90% distribution requirement and introduce partial tax-exempt measures
				④ Institutional investor requirements If the number of investors is fewer than 50, only institutional investors (defined under tax laws) are allowed to invest. In the case of a private placement, investment from general investors—such as high-net-worth individuals or overseas investors—are not allowed.	④ Allow general investors to invest even when fewer than 50 investors
Taxation / Legal				⑤ Shareholding limitation in other companies It is not permitted to invest more than 50% in another corporation. As a result, investments through the establishment of an SPC or hands-on investments, such as those typically made in PE or VC transactions, cannot be undertaken.	⑤ Allow investment corporations to hold over 50% of another entity (requires amendment of the Investment Trust Act)

(※) The pass-through tax regime and conduit requirements are explained on the next slide.

(※) Pass-Through Tax Regime / Conduit Requirements and Their Relationship to Taxable Income

- Japan's investment corporation tax regime allows investment corporations to deduct profit distributions to investors as expenses when calculating taxable income (pass-through tax regime). If the investment corporation distributes all of its income, it is not taxed at the corporate level, and taxation occurs only when investors receive distributions.
- To apply the pass-through tax regime (i.e., to allow distributions to be deductible), the investment corporation must satisfy the tax-law-based conduit requirements (*).
- Even if the conduit requirements are met, if the amount of profit distributed is less than taxable income, taxable income remains within the investment corporation and taxation occurs at the fund level.

(*) Main Conduit Requirements

1. **Distribution Requirement of Over 90%**
The investment corporation must distribute more than 90% of distributable profits.
2. **Institutional Investor Requirement (part of end-of-period investor requirements)**
At the end of the fiscal period, the investment corporation must have either 50 or more investors, or all investors must be "institutional investors" (as defined by the tax laws). For private investment corporations with fewer than 50 investors, all investors must be institutional investors.
3. **Restriction on Holding Over 50% of Another Entity**
The investment corporation must not hold 50% or more of the shares or equity of another corporation (same restriction exists under the Investment Trust Act).

⇒ These fund-level taxation rules and conduit requirements are considered obstacles to the expansion of investment corporations, and therefore proposals for improvement are made.

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Issues and Policy Proposals for Investment Corporations Explanation of Specific Measures

(1) Explanation of Specific Policy Measures

Policy Proposal①

Allow Optional Application of IFRS

(Case Assumption) Investment property acquired at 1,000 at end of Year X0. Depreciation in Year X1: 200. Fair value at end of Year X1: 1,200

Under J-GAAP

BS		PL	
Assets		Op. Revenue	...
...		Op. Expenses	...
Investment Property	1,000	Rental Exp.	
Acc. Depreciation	200	Depreciation	200
Net Book Value	800	...	
...		Net Income	...

Under JGAAP, real estate is measured at “acquisition cost less depreciation expense.” Therefore, the book value on the current period’s BS is 1,000 – 200 = 800, and depreciation expense of 200 is recognized on the PL.

Under IFRS

BS		PL	
Assets		Op. Revenue	
...		Valuation Gain	200
Investment Property	1,200	Op. Expenses	...
...		Net Profit	...
		(assuming FVTPL)	

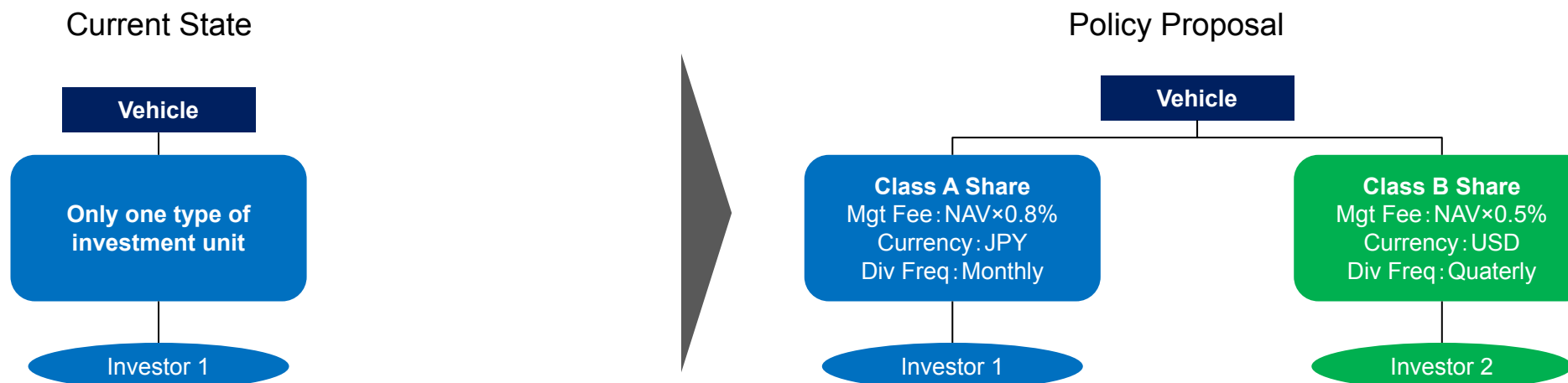
Assuming FVTPL treatment, under IFRS real estate is measured at FV. Accordingly, the BS reflects the property at its fair value of 1,200, while a valuation gain of 200 is recognized on the PL.

Current Situation and Issues	Proposed Policy Measure	Expected Effects
<ul style="list-style-type: none"> Investment corporations currently allow only J-GAAP, but there are significant differences from IFRS, which is the global standard for investment valuation. In Singapore’s VCC, Local GAAP, US GAAP, and IFRS are all permitted. 	Allow investment corporations to optionally adopt IFRS.	Applying IFRS would enhance transparency and comparability for overseas investors, making it possible to attract more investment.

(1) Explanation of Specific Policy Measures

Policy Proposal②

Allow Issuance of Multiple Unit Classes (Share Classes)



※The terms and conditions for each class are only examples. As illustrated, shares may be categorized by factors such as fee percentages, currency, and dividend frequency.

Current Situation and Issues	Proposed Policy Measure	Expected Effects
<ul style="list-style-type: none"> • Only a single class of investment units may be issued. Issuance of multiple unit classes (share classes) is not permitted under the Investment Trust Act. • In Singapore’s VCC, issuance of share classes is allowed. 	<p>Allow investment corporations to issue multiple unit classes (share classes).</p>	<p>By allowing issuance of unit classes tailored to investor attributes and needs—such as residence, currency hedging requirements, distribution frequency, or investment currency—it becomes possible to attract family offices, high-net-worth individuals, and investors with diverse needs.</p>

(1) Explanation of Specific Policy Measures

Policy Proposal③

Relax the Requirement to Distribute Over 90% of Profits and Introduce Partial Tax-Exempt Measures



Current Situation and Issues	Proposed Policy Measure	Expected Effects
<ul style="list-style-type: none"> Investment corporations must distribute over 90% of their current-period profits. Because nearly all profits must be distributed, reinvestment becomes difficult, limiting investment strategies. Any remaining portion that cannot be distributed (taxable income) becomes subject to taxation at the investment corporation level. 	<p><u>Relax the 90% distribution requirement within the conduit rules, and introduce partial tax-exempt measures for investment corporations.</u></p> <p>Specifically, revise the requirement to distribute over 90% to unitholders, and introduce tax-exempt treatment for amounts that meet certain conditions (e.g., reinvestment or asset replacement).</p>	<ul style="list-style-type: none"> Enables diverse investment strategies such as asset replacement, new investments, and reinvestment using income gains or capital gains without requiring new equity issuance or borrowing. Provides attractive tax incentives for investors and fund managers. Enhances the appeal of corporate-type funds in Japan, making them a more viable option for overseas investors

(1) Explanation of Specific Policy Measures

Policy Proposal④

Enable general investors to invest in privately placed investment corporations (by relaxing the institutional investor requirement under the conduit taxation requirements, specifically the year-end investor requirement).

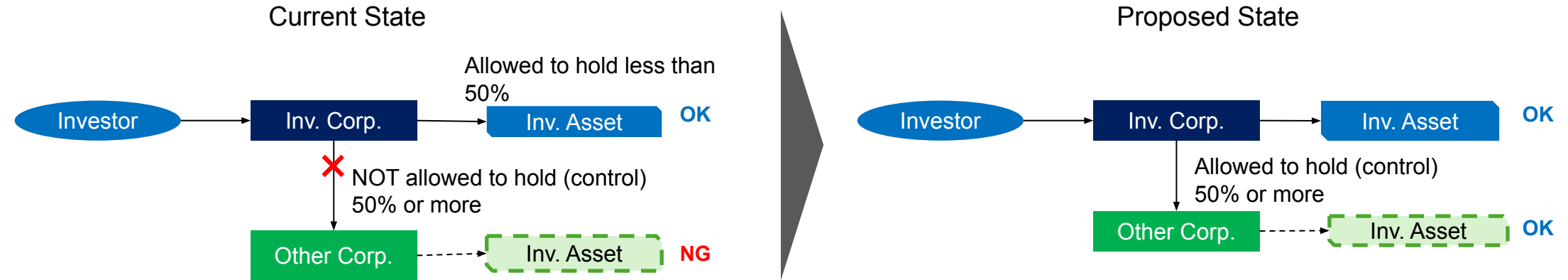


Current Situation and Issues	Proposed Policy Measure	Expected Effects
<ul style="list-style-type: none"> For privately placed investment corporations with fewer than 50 investors, all investors are currently required to be institutional investors (one of the conduit taxation requirements under Japanese tax law). No similar restriction exists under the Singapore VCC framework. 	<p><u>Relax the institutional investor requirement among the conduit taxation requirements.</u> It is proposed that privately placed investment corporations with fewer than 50 investors should also be permitted to accept investments from general investors.</p>	<ul style="list-style-type: none"> This is expected to promote the use of such structures as asset management vehicles for family offices, high-net-worth individuals, and other general or overseas investors, thereby expanding investment activity.

(1) Explanation of Specific Policy Measures

Policy Proposal⑤

Permit investment of 50% or more in the shares or equity interests of other corporations (by relaxing the restrictions on holdings of shares in other corporations under the conduit taxation requirements, together with amendments to the Investment Trust Act).



Current Situation and Issues	Proposed Policy Measure	Expected Effects
<ul style="list-style-type: none"> Investment corporations are currently prohibited from making investments of 50% or more in other corporations (including SPCs). This restriction arises under both the Investment Trust Act and the conduit taxation requirements under tax law. Under the Singapore VCC framework, there are no restrictions on ownership percentages in investment targets. 	<p><u>Relax the restrictions on holdings of shares in other corporations under the conduit taxation requirements, together with amendments to the Investment Trust Act.</u></p> <p>It is proposed that investment corporations be permitted to make investments of 50% or more in other corporations. Corresponding amendments to the Investment Trust Act would also be required.</p>	<p>This would enable flexible investment strategies such as:</p> <ul style="list-style-type: none"> Hands-on investments in PE funds (acquiring more than 50% ownership and engaging deeply in the management of portfolio companies to enhance value) Diversified investments in various asset classes through SPC structures Co-investment with third parties in specific assets, etc.

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APPENDIX

Comparison Table of Domestic Fund Vehicles and VCC

(1) Comparison between domestic fund vehicles and Singapore VCC

	LPS	Investment Trust	Investment Corporation	Singapore VCC
Governing Law	Limited Partnership Act for Investment Business	Investment Trust and Investment Corporation Act		Variable Capital Companies Act
Legal Form	Partnership-type	Trust-type	Corporate-type	Corporate-type
Supervisory Authorities	METI (for LPS Act); FSA (for Financial Instruments and Exchange Act); Ministry of Justice (for Commercial Code and Civil Code matters)	FSA		MAS ACRA
Taxation Regime	Pass-through taxation	No taxation under certain conditions	If conduit taxation requirements are satisfied, dividend distributions may be treated as deductible expenses (pass-through). If distributable profits are less than taxable income, the difference is taxed at the investment corporation level	Tax-exempt under Section 13
Restrictions on Investment Targets	Prohibition on investing 50% or more in tangible real estate, derivatives, or foreign companies	Investment in other corporations exceeding 50% is not permitted		No Restriction
Issuance of Unit Shares / Investment Units	Not Allowed	Not Allowed		Allowed
Umbrella Structure	Not Allowed	Not Allowed		Allowed
Employment of Staff	Not Allowed	Not Allowed		Allowed
Accounting Standards	Subject to the Enforcement Regulations of the LPS Act; IFRS may be used for investment valuation	J-GAAP (Investment Trust Accounting Rules)	J-GAAP (Investment Corporation Accounting Rules)	Local GAAP US GAAP IFRS