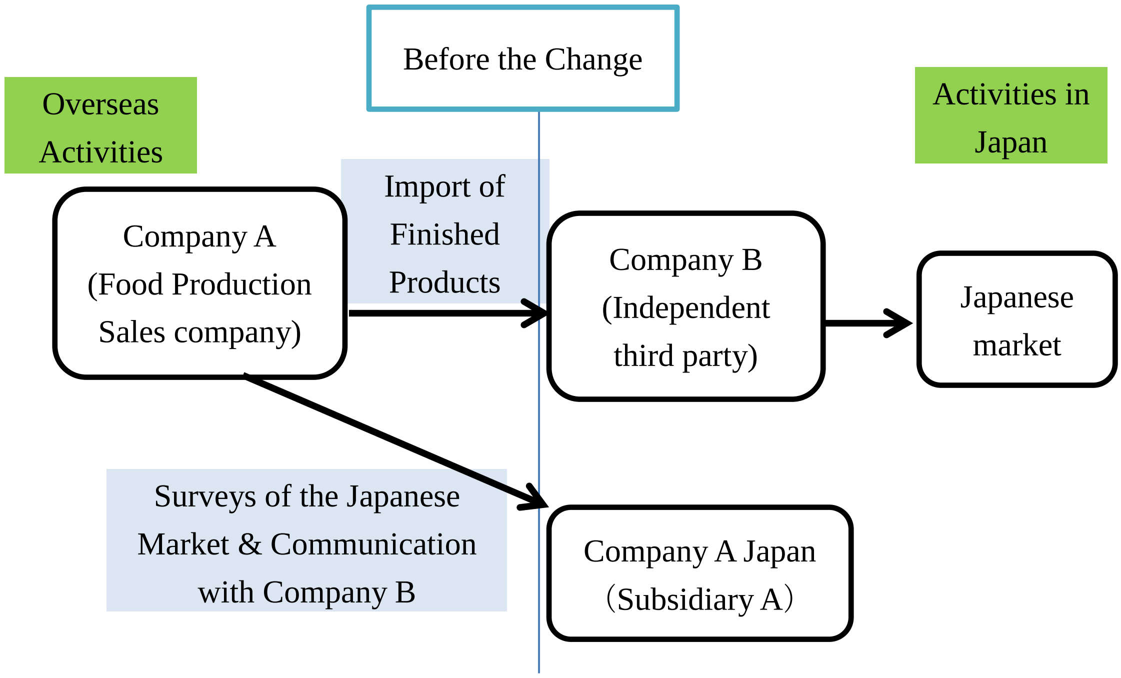
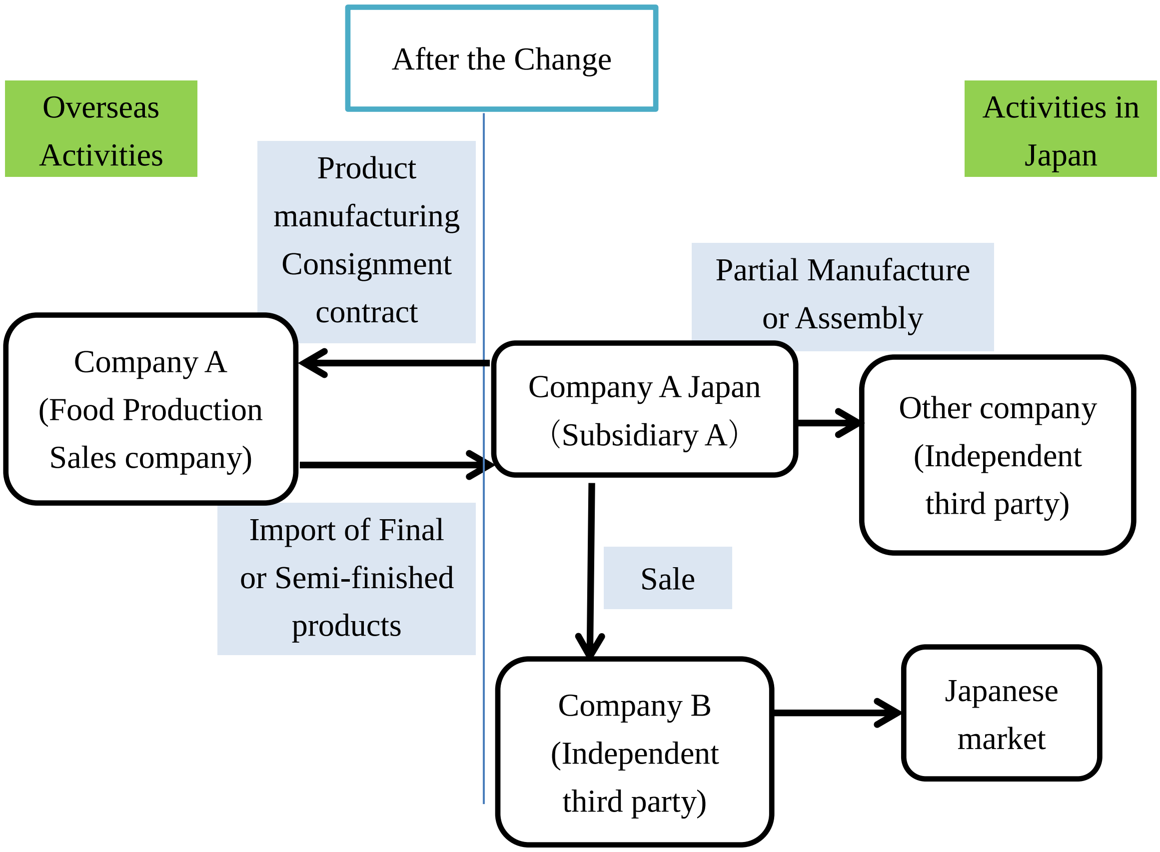
Case 3 – Helping the Japan Tax Authority Understand the Results of Transactional Restructuring

A multinational food manufacturing & sales company group decided to invest more heavily in the Japanese market by enlarging the role of its Japanese subsidiary in the overall manufacturing process. The Japanese subsidiary became newly responsible for manufacture, research and development, logistics, finances, marketing, and the sale of products in Japan; but the resulting decline in imports from the multinational group caused a corresponding decline in customs revenue for the Japanese tax authorities, which in turn triggered a significant audit.

Diagram B: Before and after the changes; decreasing imports while increasing multinational investment in its Japanese subsidiary





KLO was engaged to help with the audit. If the company failed to give solid reasons behind the reduction in its self-reported customs taxes, there was a danger of the tax authority imposing significantly more customs duties than those that the company had reasonably expected. KLO developed models of the Japanese subsidiary's imports before and after the change, with the support of well-documented figures; and reassured the tax authority that the revenue lost by customs tariffs would be recovered through corporate taxes on the increased profits generated by the subsidiary in Japan. Part of our sensitive approach to the problem involved repeated visits to the tax authority with charts and presentations such as the one in Diagram B. After these substantial explanations, the tax authority was satisfied with KLO's models, and the audit was favorable.