

Rule of Law and Japanese Tax Law*

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Preface

It is an honor and pleasure to speak at the Annual Conference of AOTCA. The title of my speech is “Rule of Law and Japanese Tax Law.”

The most important element of rule of law in taxation is the principle of “no-taxation-without-representation”: that taxpayers are not required to pay taxes which lack a statutory basis. Historically, the principle that taxes cannot be imposed without the consent of those who would be taxed can be traced back to the Magna Carta of 1215. With the development of Parliament, this principle was transformed into no-taxation without the consent of Parliament (the Petition of Rights of 1629), and finally established in the Bill of Rights of 1689 in England. The French Declaration of Citizens Rights of 1789 also adopted this principle. No-taxation-without-representation was of course the slogan of the Boston Tea Party.

I. Introduction

1. Pre-War Trends

The first modern constitution of Japan (hereafter referred to as the Meiji Constitution), was enacted in 1889 under the reign of the Meiji Emperor. The Meiji Constitution adopted the separation of powers, and accordingly implied the “Rechtsstaatsidee” (an idea similar to rule of law) of European continental nations. Under the Meiji Constitution, German books on public law including Otto Mayer’s “Deutsches Verwaltungsrecht” were widely read by legal scholars in Japan, and such

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concepts as “rechtssatzschaffende Kraft”, “Vorrang des Gesetzes” and “Vorbehalt des Gesetzes” were well known to them.¹

The Meiji Constitution contained two articles on taxation: Article 21 provided that Japanese people were subject to tax according to statutes. Article 62 prohibited the imposition of new taxes, or the modification of existing tax rates, unless laid down in a statute. These articles, and Article 62 in particular, were apparently expressions of the Western idea of the “rule of law” and the “Rechtsstaatsidee”. Count Hirobumi Ito, the central figure behind the Constitution and Chairman of the Privy Council, wrote about the article: “It is a great and beautiful fruit of the constitutional government and promotes directly the happiness of the people to require the consent of the Diet in imposing new taxes, and not to leave the matter to the arbitrary decision of the executive.”²

Scholars expressed similar opinions. For instance, Tatsukichi Minobe wrote, in essence, as follows in 1923:³

Taxes should be governed by statutes. This is provided explicitly by Article 62 of the Constitution. The article shows that taxes cannot merely be based upon executive orders but requires the enactment of a statute containing the object of the tax, the tax base, the tax rate, and the taxpayer. In other fields of administration, it is not unusual for statutes to delegate the matters to be provided by statutes to the executive, but in taxation it is usual that statutes refrain from delegation and contain all the above-mentioned elements themselves.

Academic research in tax law in pre-war times started with the work of the late Shozaburo Sugimura. In 1931, he translated the second edition of Albert Hensel’s “Steuerrecht” into Japanese,⁴ and published a systematic book entitled “Tax Law” in 1939.⁵ By these works, the principle of sozei-horitsu-shugi (literally, tax-statute-principle; identical to the principle of “Gesetzmäßige Besteuerung”; hereafter referred to as the principle of statute-based taxation) and the concept of kazeiyoken (Steuertatbestand; hereafter referred to as tax-liability prerequisite) were

¹ Otto Mayer’s “Deutsches Verwaltungsrecht” was translated into Japanese by Professor *Tatsukichi Minobe* in 1903. As a systematic research of Otto Mayer’s administrative law theory, cf. *Hiroshi Shiono*, *The Structure of Administrative Law Theory of Otto Mayer* (1962).

² *Hirobumi Ito*, *Commentaries on Constitution* (1889).

³ Cf. *Tatsukichi Minobe*, *System of Administrative Law*, Book Two, p.353 et seq (1924).

⁴ *Shozaburo Sugimura*, *Theory of German Tax Law* (1931). Professor *Sugimura* was Professor of Administrative Law at the University of Tokyo, and extended his research to tax law.

⁵ *Shozaburo Sugimura*, *Tax Law* (1939)

introduced, analyzed and clarified in Japan for the first time.

However, since courts were not entitled to review the constitutionality of statutes under the Meiji Constitution, theoretical research and analysis of Article 62 and the principle of statute-based taxation were not subject to further development.

Also, since Japan embarked on her modernization much later than Western nations, she had to rely heavily on a strong and stable bureaucracy in order to promote modernization, i.e., to catch up to Western nations quickly and to develop industry efficiently. Therefore, one characteristic element of Japan's modernization was that within the three branches of the government, the executive gained the strongest power, and decision-making was almost entirely monopolized by bureaucrats. This development resulted in the fact that usually statutes were rather simple and covered basic matters, and many important decisions were delegated to executive order. Despite Minobe's claim to the contrary, the field of tax law was no exception. Tax statutes, too, usually covered basic matters, and delegated many important matters to Cabinet Orders and Ministerial Orders.

2. Post-War Trends

Things have changed after World War II. The current Constitution of Japan was enacted in 1946 and promulgated in 1947. Again, it contains two articles on taxation: Article 30 provides that the people have a duty to pay tax according to statutory provisions; and Article 84 prevents the government from imposing new taxes, or modifying existing ones, unless permitted by statute or under such conditions as a statute may prescribe. These two articles are similar to the two Meiji Constitution articles mentioned above. The basic difference between the two constitutions is that under the current Constitution, the courts are empowered to review the constitutionality of the provisions of statutes, executive orders and administrative actions (Article 81). Moreover, Article 41 of the Constitution provides that the Diet is the supreme branch of the Government and the sole legislative body.

Taxpayers soon started to dispute the constitutionality of various tax provisions in court. Various issues have been raised concerning different provisions of the Constitution, and court decisions have accumulated concerning the conformity of a multitude of tax provisions with different constitutional provisions.

One of the most disputed issues was whether the provisions of tax law complied with Article 84 of the Constitution. On this issue, the Supreme Court repeatedly suggested in dicta that the principle of statute-based taxation required legislators to lay down clearly the prerequisites for tax liability, and the procedure of tax

assessment and tax collection in Acts of Parliament.⁶

Incidentally, tax law education and research as an independent field of jurisprudence developed in Japan in the 1950s. This was directly due to the “Report on Japanese Taxation” by the Shoup Mission of 1949-50 which recommended that tax law should be taught at the law faculties of universities and that chairs of tax law should be created for that purpose.⁷ Since then, the number of scholars specializing in tax law has gradually increased. Consequently, the analysis of Article 84 of the Constitution (and the principles embodied in it) has gained more and more importance.⁸

For instance, I have published two articles, entitled “Citizens and Tax” and “Basic Principles of Tax Law”, respectively.⁹ In these articles, I traced the history of the principle of statute-based taxation in England and examined the contents and significance of that principle. Likewise, I examined the contents and significance of the principle of statute-based taxation and related matters. I concluded that the principle of statute-based taxation originated in two different but related values and therefore should serve these two values at the same time. The first was the traditional constitutional value of “no taxation without representation”. This value demands the supreme role of Parliament in tax legislation. The second was the need for legal stability and predictability (“Brechenbarkeit”) in taxation. Since taxes are imposed today on virtually all economic activity and the actual liability is substantial, it is indispensable for a reasonable person making any economic decision to take into account its tax effects. Accordingly, legal stability and predictability in taxation is what Adam Smith called “certainty” in his “Wealth of Nations¹⁰.”

With regard to these two values, and basically in accordance with German and Anglo-American theories, I divided the principle of statute-based taxation into the

⁶ For instance, Decision of March 23, 1965, Supreme Court Civil Cases Reporter, vol.9, no.3, p.336 Decision of March 27, 1985, id., vol.39, no.2, p.247

⁷ Cf. *Shoup Mission*, Report on Japanese Taxation, vol.4 p.D-67 (1949); id., Second Report on Japanese Taxation, p.79 (1950).

⁸ As examples of systematic work by administrative law professors, cf. *Shozaburo Sugiyama* An Outline of Tax Law (1950); *Jiro Tanaka*, Tax Law (1st edition 1968). As examples of systematic work by tax law professors, cf. *Ichiro Nakagawa*, System of Tax Law Theory (1968); *Keiji Kiyonaga*, Tax Law (1st edition 1970); *Hiroshi Kaneko*, Tax Law (1st edition 1976); *Ryuichi Arai*, Basic Theory of Tax Law (1st edition 1974); *Hiroshi Kaneko*, Lectures on Tax Law (1st edition 1970); *Takemichi Hatakeyama*, Tax Law (1st edition 1977).

⁹ *Hiroshi Kaneko*, Citizen and Tax, in “Iwanami Lectures on Modern Law”, vol.8, edited by Ichiro Kato, p.307 (1967); id., Basic Principles of Tax Law, in “Lectures on Tax Law”, vol. I, edited by Hiroshi Kaneko et al., p.195 (1974).

¹⁰ Cf. *Adam Smith*, An Inquiry into the Nature and Causes of the Wealth of Nations vol. II, p.424 (London 1776).

following six sub-principles:¹¹

- (1) the principle that the prerequisites for tax liability (“*Steuertatbestand*”) and the procedure of assessment and collection of tax should be specified in statutes (principle of reservation to statutes);
- (2) the principle that the prerequisites for tax liability and the procedure for the assessment and collection of taxes should be precisely provided (principle of preciseness);
- (3) the principle of prohibition of retroactive legislation (principle of non-retroactivity);
- (4) the principle that tax statutes should be strictly enforced (principle of legality);
- (5) the principle of due process in taxation; and
- (6) the principle that the right of taxpayers should be protected by a formal litigation system (principle of judicial protection of the taxpayers’ right).

Today, I would like to introduce to my foreign audience the present situation concerning the rule of law in Japanese taxation. Toward that end, I will introduce and examine both court decisions and scholarly opinion concerning the first three sub-principles, and briefly explain the last three sub-principles.

II. Present situation of sub-principles

1. Principle of Reservation to Statutes

(1) General Observations

Article 73 (vi) of the present Constitution provides that the provisions necessary for the enforcement of statutes can be laid down in orders of the executive branch without any statutory delegation. On the other hand, it is also the legal consensus that Article 84 requires that the prerequisites for tax liability and the procedure for the assessment and collection of tax be provided by statutes. As mentioned above, the Supreme Court has upheld this interpretation repeatedly.¹²

The most disputed subject concerning this principle has been the relation

¹¹ Cf. *Hiroshi Kaneko*, *Citizen and Tax*, op. cit., p.316 et seq.; id., *Basic Principles of Tax Law*, op. cit., p.204 et seq.; id., *Tax Law* (20th rev. ed. (2015), p.73)

¹² Cf. note 6.

between statutes and executive orders (Cabinet and Ministerial Orders). It is clear that the executive may not specify the prerequisites for tax liability and the procedures for assessing and collecting the tax unless Parliament has delegated that authority to it (Vorbehalt des Gesetzes). Also, it is apparent that provisions in orders violating or contrary to statutory provisions are not valid (Vorrang des Gesetzes).

It is the consensus among constitutional law scholars that delegation to the executive is implicitly permitted by the present Constitution.¹³ Also, as a matter of fact, it is difficult completely to deny the necessity for delegation. Needless to say, with regard to Article 41 and 84 of the Constitution, the delegation should not be general and blanket, but concrete and precise.¹⁴ Therefore, the problem was to what extent and under what conditions statutes can delegate to executive order the prerequisites for tax liability and rules regarding the procedures for assessment and collection. This point was disputed very much because in spite of Articles 84 and 41 of the Constitution the traditional pattern of legislation continued even after the enactment of the Constitution; that is, tax statutes specified only basic matters and delegated other (sometimes very important) matters to Cabinet and Ministerial orders. The following paragraphs aim at examining some important cases.

(2) Some Court Decisions

(a) Musical Instruments Case

Decision of the Supreme Court of June 18, 1964, Supreme Court Criminal Cases Reporter, vol.18, no.5, p.209¹⁵

In a famous criminal case, a piano and organ manufacturing corporation and its chief executive were prosecuted for the evasion of the commodity tax. On its commodity tax return, the corporation omitted a substantial part of the revenue from the sale of organs. The commodity tax was a signal-stage selective sales tax. The Commodity Tax Act listed musical instruments as taxable objects in general but delegated to Cabinet Order the scope of taxable musical instruments. Based on this

¹³ Cf. *Toshiyoshi Miyazawa*, Commentaries on the Constitution of Japan, p.574 et seq. (1978); *Jiro Tanaka*, Theory of Administrative Law-General Part, p.364 (1957); *Masami Ito*, Constitutional Law, p.412 (new ed. 1990); *Nobuyoshi Ashibe*, Constitutional Law, p.265 (rev. ed. 1999); *Koji Sato*, Constitutional Law, p.147 (3d ed. 1995).

¹⁴ Cf. *T.Miyazawa*, op. cit., p.577; *J.Tanaka*, op.cit.; p.367; *M.Ito*, op.cit., p.662; *N. Ashibe*, op. cit, p.265 et. seq.

¹⁵ As a short comment on this case, cf. *Setsuo Kinashi*, Bar Journal, vol.16, no.8, p.1190. Cf. also *Hiroshi Kaneko*, Basic Principles of Tax Law, op. cit., p.208 et seq.

delegation, the Cabinet Order listed organs as taxable items. The accused asserted that this delegation violated Article 84 of the Constitution and the principle of statute-based taxation embodied in it, and therefore, that the provision of delegation and the provision of the Cabinet Order under it were invalid. Based on this argument, they asserted that these provisions could not be applied to them and, consequently, that their behavior did not constitute tax evasion.

The decision of the Supreme Court of June 18, 1964 flatly rejected these assertions, holding that because the Commodity Tax Act enumerates the taxable commodities concretely, and clarifies the scope of taxable commodities, the relevant provisions of the Act and the Order are not unconstitutional. Because an organ is a musical instrument, and because the delegation in this case was neither general nor blanket, no objection was expressed by constitutional law scholars to this decision. One problem with this decision was that it did not explore further the limits to permissible and impermissible delegation.

(b) Bonus for Executive-Employees Case

Decision of the Osaka High Court of June 28, 1968; Administrative Cases Reporter, vol.19, no.6 p.1130)¹⁶

1st Instance Court: Decision of the Osaka District Court of May 30, 1966; Administrative Cases Reporter, vol.17, no.5, p.591)¹⁷

This interesting decision by the Osaka High Court concerns the case of a family company, i.e., a corporation where 50% or more of the outstanding shares are owned by three shareholders and their specially related persons (hereafter referred to as dominant shareholders and specially related persons). From 1958 to 1961, the corporation paid bonuses to four dominant shareholders and their specially related persons, who had dual status as executives and employees, for their service as employees. On its corporate income tax return, the corporation deducted the bonus to the specially related persons as expense. The District Tax Office director assessed a deficiency. He reasoned that bonuses paid to the executive-employees of a family corporation could not be deducted

¹⁶ As the comments on this decision, cf. *Ichiro Nakagawa*, *Steuer*, no.77, p.6; Hiroshi Kaneko, *Research of Local Autonomy*, vol.46, no.4, p.138; *Kazuo Yamanouchi*, *Studies on One Hundred Tax Law Cases* (2ed edition), edited by *Hiroshi Kaneko*, p.14; *Yoshinobu Kitamura*, *Studies on Hundred Tax Law Cases* (3rd edition), edited by *Hiroshi Kaneko*, *Tadatsune Mizuno*, and *Minoru Nakazato*, p.8.

¹⁷ For comments on this decision, cf. *Tadashi Murai*, *Studies on One Hundred Tax Law Cases* (1st edition), edited by *Ichiro Ogawa and Hiroshi Kaneko*, p.14; *Ichiro Nakagawa*, *Steuer*, no.52, p.1; and the comments listed up at the end of Murai's comment.

as expenses, according to Corporate Tax Cabinet Order (hereafter referred to as CTCO) at that time.

Until the comprehensive amendment of 1965, the Corporation Tax Act (hereafter referred to as CTA) was rather simple as far as the substantive rules were concerned. Article 9(1) of the CTA provided that the amount of income of a corporation equaled the amount of total revenue less total expense. Article 9(2)-(7) and several other articles specified a few other basic items of revenue and expense. Then Article 9(8) provided that matters not provided by the CTA were to be specified in the CTCO.

Under this delegation, various items of revenue and expense were provided by the CTCO. One group of provisions covered the treatment of bonuses to executives. First, Article 10-4 provided that bonuses paid to executives were not deductible, whereas bonuses paid to executive-employees could be deducted as expenses, as far as the part allocable to their service as employees was concerned. Already before World War II, both the Japanese Corporation Law and the Corporation Tax Act started to treat bonuses paid to executives as the disposition of profits rather than an expense. This categorization has not changed since (however, by amendment to the CTA in 2006, bonuses paid to executives are now deductible under certain conditions). Therefore, it could be said that this provision was a restatement of an established and reasonable interpretation and did not require explicit delegation in the CTA.

Second, Article 10-3(6)(iv) excluded from the scope of executive-employees “the executive-employees of family companies, who are the dominant shareholders or their specially related persons.”

The deficiency assessment was based on these provisions. The corporation brought suit in Osaka District Court against the District Tax Office Director, claiming invalidation of the assessment, and asserted that the assessment was illegal because Article 10-3(6)(iv) violated Article 84 of the Constitution as well as Article 9(1) of the CTA, and that it exceeded the scope of the delegation in Article 9(8) of the CTA.

The Osaka District Court sustained the claim of the corporation and invalidated the deficiency assessment except the part of the bonus which the Court thought was attributable to the services of these executive-employees as executives (Decision of May 30, 1966). The essence of the Court’s decision was as follows:

- (i) Dominant shareholders, and their specially related persons, of a family company can be employees of that company.
- (ii) For the calculation of the company’s income, bonuses paid to these persons in their capacity as employees are deductible.
- (iii) Article 10-3(6)(iv) of the CTCO denies the dual status of the executive

employees who are the dominant shareholders or their specially related persons, of a family company. Accordingly, bonuses paid to them for their service as employees are not deductible. This is the same as imposing a corporation tax on the amount of bonuses paid to employees, and consequently the same as creating a new tax liability.

- (iv) If it was necessary to adopt this treatment for policy reasons, it should have been specified by statute. This follows from the principle of statute-based taxation.
- (v) Such a basic provision cannot be provided in the CTCO, based on Article 9(8) of the CTA.
- (vi) Therefore, Article 10-3(6)(iv) of the CTCO violates the principle of statute-based taxation, and cannot be applied.

The director of the District Tax Office appealed to the Osaka High Court, but the court sustained the corporation's claim and dismissed the appeal. However, the reasoning differed from that given by the District Court (Decision of June 28, 1968).

After rejecting the director's assertion that Article 10-3(6)(iv) of the CTCO was an interpretative provision, on the ground that the article seriously affected the rights and duties of taxpayers, the High Court held that the relevant CTCO provisions should be understood as based on the delegation of Article 9(8) of the CTA. Then, the High Court held:

“From the viewpoint of the principle of statute-based taxation, legislative delegation provisions should specify the purpose, content, and scope of any delegation. The legislature may not delegate through general and blanket provisions regarding such prerequisites for tax liability as items of revenue and expense. Accordingly, Article 9(8) of the CTA should not be interpreted as having granted the CTCO broad discretion to determine the prerequisites for tax liability. Anyway, it is impossible for the CTCO to deny the deductibility of expenditures which have the nature of expenses and have been treated as deductible expenses in both theory and practice.”

Because the District Tax Office Director did not appeal to the Supreme Court, the case ended with the decision of the High Court.

Incidentally, after the decision of the District Court appeared, I published an

article entitled “Citizens and Tax” in 1966.¹⁸ After having researched German theory on delegation of legislation, I argued that under the Japanese Constitution too, the test for the distinction between permissible concrete and precise delegation and impermissible general and blanket delegation should be whether the purpose (Zweck), content (Inhalt) and scope (Ausmaß) of the delegation are clear in the delegating statute itself.¹⁹ I would count it an honor if this article had any influence on the Osaka High Court and bridged German and Japanese theory.

The decision of both the Osaka District Court and the Osaka High Court are interesting and can be appreciated from the viewpoint of the principle of statute-based taxation. I suspect that the High Court's holding has had a bigger effect in moving the weight of policy-making from the executive branch to the Diet.

Having been influenced by this and other cases in which the validity of CTCO provisions was disputed from the viewpoint of the statute-based taxation, the legislature amended the CTA extensively in 1965. Many CTCO provisions, including that on the bonuses for executives and executive- employees, were transferred to the CTA.

(c) Registration Tax Refund Case

Decision of the Tokyo High Court of November 28, 1995; Monthly Litigation Reporter, vol.42, no.11, p.2789²⁰

1st Instance Court: Decision of the Chiba District Court of February 22, 1995,. Monthly Litigation Reporter, vol.42, no.11, p.2801

The plaintiff in this case was a small timber corporation and the member of a trade association. The association's purpose was to gather medium-and small-sized timber enterprises in an industrial zone near the Kisarazu port in Chiba Prefecture.

The plaintiff purchased land and a building on it in the zone from the association and registered the purchase at the relevant registration office. It paid the registration tax to the office. The amount of tax was calculated according to the Registration Tax Act. About two months later, the corporation learned about Article 78-3 of the Special Tax Treatments Act which provided for a reduced tax rate on the registration of the purchase of real estate located in a zone for gathering medium-and small-sized enterprises. If the reduced rate had been applied, the amount of tax would have been

¹⁸ Cf. supra foot note 9.

¹⁹ Cf. *Hiroshi Kaneko*, Citizen and Tax, op. cit., p.316. Cf. Decision of German Constitutional Court on Firma Salamander Case. Urteil des Zweiten Senats vom 5 März 1958, BVerfGE 7.2.82

²⁰ As a comment on this decision, cf. *Tutomu Nunoda*, Juristo, no.1113, p.25.

about 7.7 million yen less than the amount the plaintiff actually paid. The plaintiff demanded that the registration office refund the overpaid tax. However, the office rejected the claim. It argued that at the time the plaintiff applied for the registration, it had not attached a certificate from the prefectural governor as specified by Ministerial Order. The corporation quickly obtained the certificate from the governor and submitted it to the registration office. It asked the office director to send a formal notice of refund to the district tax office director. Nevertheless, for the reasons above, the director rejected the request. The corporation then sued in Chiba District Court, claiming that the Japanese government should refund the amount of the over-paid tax with interest.

At the time, Article 78-3(1) of the Special Tax Treatments Act provided that in cases like this, instead of the tax rate of 44/1000 laid down in the Registration Tax Act, the reduced rates of 12/1000 (for land) and 10/1000 (for buildings) should apply “according to the provisions of Cabinet Order”. Under this provision, Article 42-9(3) of the Special Tax Treatments Cabinet Order provided that the reduced rates would apply only when registration was made within a month after purchase of real estate “according to the provisions of ministerial order”. Under this provision, Article 29(1) of the Special Tax Treatments Ministerial Order provided that for the application of the reduced rates, taxpayers should attach the certificate of the governor to the application form for registration.

The government denied that it owed a refund. The corporation had not satisfied the requirement that it attach the governor's certificate to its application form, it explained. Accordingly, the reduced rates did not apply and the firm was not entitled to a refund. Against this assertion, the corporation raised several grounds. Most importantly, it argued that the delegation provision of Article 78-3(1) of the Special Tax Treatment Act was extremely general and broad. Had the legislature intended to delegate to the Cabinet Order the task of imposing requirements other than those provided in the statute itself, such delegation would have violated the principle of statute-based taxation. Accordingly, the procedural requirement in the Ministerial Order was invalid and inapplicable.

The Chiba District Court sustained the corporation's claim, and ordered the government to refund the over-paid tax with interest (Decision of February 22, 1995). The important points of the holding of the Court were:

- (i) The principle of statute-based taxation also applies to preferential tax treatments.

- (ii) Article 78-3 says nothing about procedural requirements. Other provisions of the Special Tax Treatments Act usually contain the words “so long as taxpayers follow the procedures provided by ministerial order”. Therefore, it is difficult to say that Article 78-3 requires taxpayers to follow some procedure as the condition for receiving the reduced rates. Those parts of the cabinet and ministerial orders imposing the additional procedural requirement thus have no legal effect and are inapplicable.
- (iii) Even if Article 78-3 did require a certain procedure, provisions like “according to the provisions of cabinet order” would constitute a blanket delegation in violation of the principle of statute-based taxation.

The Government appealed to the Tokyo High Court. The High Court sustained the claim of the corporation and dismissed the appeal (Decision of November 28, 1995). The holding of the High Court was substantially similar to, but different in some respects from, that of the District Court. The essential part of the holding of the High Court was as follows: In view of Article 84 of the Constitution, statutory delegations to orders are permissible only when the delegations do not violate the principle of statute-based taxation. Under this principle, a delegation of the details of tax collection procedure is permitted, and concrete and precise delegations are permitted. However, if procedural requirements are delegated, the statute itself must state something about it and explicitly delegate the procedural details to an order. Under the principle of statute-based taxation, additional requirements cannot be created by interpretation without a clear statutory delegation. Consequently, the abstract and unlimited delegation of Article 78-3(1) providing "according to the provisions of cabinet order" should be interpreted narrowly. It must not be construed to imply any authority to add procedural requirements to the application of reduced rates. Therefore, Article 29(1) of the Special Tax Treatments Ministerial Order is invalid insofar as it imposes additional procedural requirements.

The Government did not appeal to the Supreme Court. Therefore, the case ended with the decision of the High Court. Incidentally, Article 79-3 of the Special Tax Treatments Act was amended in 1996 in accord with the holdings of the courts.

2. Principle of Preciseness

This principle is a corollary to the principle of reservation to statutes. This is because if a statutory provision were so vague as to give discretion to tax authorities, it would generate the same result as a general and blanket delegation.²¹

As in other countries, Japanese tax statutes often use unclear or vague expressions or concepts (“unbestimmte Rechtsbegriff”). Among scholars, the opinion prevails that these expressions and concepts do not violate the principle of preciseness and are not unconstitutional if three tests are satisfied.²² The first is that they are not so unclear or vague as to give discretion to tax officers in effect. The second is that their meaning can be made clear by interpretation. This is the other side of the coin to the first test. The third is that the unclear or vague expressions result from the need to maintain equity between taxpayers or to realize other reasonable policy objectives.

Two examples will be introduced here -- one from the substantive law, and the other from procedural law.

Example 1: Article 132(1)(i) of the Corporation Tax Act provides that the director of a district tax office may disregard the acts or accounts of family companies, if these acts or accounts “unduly” reduce their corporate tax burden. “Unduly” is an imprecise term. However, family companies are dominated by a few shareholders, and they can sometimes take actions that substantially reduce the firm's tax burden. Therefore, this kind of provision is necessary and reasonable to keep equal the tax burdens among corporations. It is understandable that the Supreme Court held that this provision was not vague, did not violate the principle of preciseness, and therefore was not unconstitutional (Decision of April 21, 1978).²³ This does not mean that “unduly” could be loosely interpreted, of course. Rather, to prevent any abuse of power, it should be interpreted rigidly.²⁴

Example 2: Article 234 of the Individual Income Tax Act (at present article 74-2(1)(2) of the General Tax Procedure Act) provided that, “when necessary,” tax officers may audit taxpayers and examine their books and records. All other tax statutes (at present, article 74-2~74-6 of General Tax Procedure Act)

²¹ Cf. *Hiroshi Kaneko*, Tax Law (20th rev. ed. (2015)), p.79; id., Basic Principles of Tax Law , op. cit., p.218 et seq.

²² Cf. *Hiroshi Kaneko*, Tax Law (20th rev. ed. (2015)), p.79 et seq.; id., Basic Principles of Tax Law , op. cit., p.218 et seq.

²³ Monthly Litigation Reporter, vol.24, no.8, p.1694.

²⁴ Concerning this provision, cf. *Hiroshi Kaneko*, Tax Law (20th rev. ed. (2015)), p.470 et seq.

contained similar provisions. The Supreme Court held that because the expression “when necessary” does not give discretion to tax officers, and its meaning can be clarified by interpretation, it did not violate the principle of preciseness and was not unconstitutional (Decision of July 10, 1973).²⁵

In almost all cases in which the issue of preciseness was disputed, court decisions have held that the provisions at issue did not violate the principle of preciseness.

3. Principle of Non-Retroactivity

(1) General observations

Concerning the problem of whether retroactive legislation in the field of administrative law is permissible under the Japanese Constitution, a prominent scholar wrote in the late 1950s that retroactive legislation was not unconstitutional if it appropriately promoted legislative policy.²⁶ However, tax law scholars started to assert around the middle of the 1960s that retroactive tax legislation was unconstitutional to the extent that it adversely affected the interests of taxpayers.

For instance, in 1966 I wrote:²⁷

“The prohibition of retroactive legislation should be recognized as an element of the principle of statute-based taxation. Although it is permissible to change the content of tax liability through ex-post legislation to the advantage of taxpayers, it is not permissible to change it to their disadvantage. When people engage in various economic transactions or make decisions, they refer to the tax statutes at the time of their activities to check their tax consequences. In doing so, they trust that taxes will be imposed according to the statutes at the time. To betray their trust through ex-post legislation seriously injures the predictability and legal stability (certainty) that are the very objective of the rule of law. There is the position that, because the Constitution does not clearly prohibit retroactive tax legislation similar to “nulla poena sine lege,” the prohibition of retroactive legislation is not a constitutional principle but merely a

²⁵ Supreme Court Criminal Cases Reporter, vol.26, no.9, p.554. As examples of the comments of this decision, cf. *Yoriaki Narita*, *Studies on One Hundred Tax Law Cases*(3rd edition), p.168; *Hiroshi Kaneko*, *Journal of Court Decisions*, no.172, p.151.

²⁶ Cf. *Jiro Tanaka*, *Theory of Administrative Law-General Part*, p. 164 et seq. (1957).

²⁷ *Hiroshi Kaneko*, *Citizen and Tax*, op. cit. p. 317; *id.*, *Basic Principles of Tax Law*, op. cit., p. 225 et seq.; *id.*, *Tax Law* (20th rev. ed. (2015)) p.110.

principle of legislative policy. However, in view of the economic function and significance of the principle of statute-based taxation, it should be recognized that Article 84 of the Constitution implies the prohibition of retroactive tax legislation.”

Modern tax scholars generally believe that retroactive legislation violates the principle of statute-based taxation. The case to be described in the following section is an interesting example. However, concerning periodic taxes like corporate and individual income taxes, scholars and court decisions tend to suggest that the government may apply statutes or ordinances amended during the period retroactively to the beginning of that period.

(2) Some Court Decisions

(a) Okinawa Commodity Tax Case

Decision of the Fukuoka High Court, Naha Branch of October 31, 1973; Monthly Litigation Reporter, vol.19, no.13, p220

1st Instance Court: Decision of the Naha District Court of April 2, 1969; Monthly Litigation Reporter, vol.19, no.13, p231

The case concerned the Okinawa commodity tax at the time when Okinawa was still occupied by the United States. The plaintiffs were trading companies that imported certain kinds of fish into Okinawa. At the time, the Okinawa Commodity Tax Act (Order No.17 of the United States Chief Commander, issued on November 27, 1958) listed “raw fish” as a taxable commodity. Under this category, various species of fish were enumerated but the species which these corporations imported were not included. Nevertheless, the firms paid the commodity tax on the fish they imported. The facts are not clear, but they asserted that they paid it only because the tax authorities demanded that they do so, not because of any misjudgment.

In 1964, the Commodity Tax Act was amended (Third Amendment to Order No.17) and the species of fish the corporations imported and paid tax on were added to the list of taxable fish. At the same time, the amendment provided that it did not change the law: the commodity tax had been properly imposed on these species in the past even though they had not appeared on taxable list.

The corporations sued in Naha District Court, demanding that the Japanese government refund the commodity tax they had paid on the fish. They asserted that the 1964 amendment imposing the tax on commodities that had not been listed earlier

amounted to retroactive legislation. It violated the Executive Order of the U.S. President protecting the property of the people of Okinawa.

The government asserted that (1) the enumerated fish were just examples, and that the fish which the corporations imported were also included, and (2) since the corporations shifted forward the burden of tax by including it in the sales price of the fish, they actually did not have any loss to recover.

The District Court sustained the second assertion of the government and dismissed the claim of the corporations. The corporations appealed to the Fukuoka High Court and again asserted that the amendment of 1964 was retroactive legislation violating the Presidential Order. The High Court granted the appeal, and ordered the government to refund the taxes paid. The Court held that the fish enumerated in the 1958 Act were not simply examples. Rather, the list limited the scope of taxable fish. The Court also held that the 1964 amendment constituted retroactive legislation. Given the principle of statute-based taxation, the government could enact retroactive taxation only when an amendment of the law was scheduled and the taxpayer could predict the amendment at the time of he undertook his activities. Only then, the Court explained, would legal certainty not be seriously compromised. Here, however, the legislation aimed to legalize retroactively the imposition of tax on non-taxable commodities for several years. This exceeded the permissible bounds.

Concerning the assertion of the government that there was no loss for the corporations to recover, the Court held that, although the commodity tax was an indirect tax and the burden thereof was usually shifted to consumers, this did not justify any denial of a taxpayer's right to a refund of the tax he paid erroneously. After all, commodity sales prices were decided by market competition. Since the government did not appeal to the Supreme Court, the litigation ended with the decision of the High Court.

This decision was widely lauded for establishing and developing the principle of statute-based taxation. However, there is one published court decision which held that retroactive legislation in taxation was not unconstitutional (see below).

(b) Special Land-Holding Tax Case

Decision of the Osaka High Court of August 30, 1977, High Court Civil Cases Reporter, vol.30, no.3, p.217²⁸

In 1969, the income tax on capital gains on the sale of land by individual

²⁸ As a comment on this case, cf. *Yoshikazu Miki*, *Zeikeitsuushin*, vol.39, no.15, p.376.

landowners was drastically reduced, in order to increase the supply of land and to lower its price. However, because of the speculative purchase of land by corporations and individual real estate entrepreneurs, the price of land substantially rose (which obviously was opposite to the stated policy purpose). To solve this problem, the so-called Special Land-Holding Tax (the SLHT) was introduced in 1973 as a municipal tax imposed on land owned by corporations and individual real estate entrepreneurs and purchased on or after January 1, 1969.

Some taxpayers sued in the Osaka District Court, contesting the application of the SLHT. After their claim was dismissed by the District Court, they appealed to the Osaka High Court. One of their claims was that it violated the prohibition of retroactive legislation to impose the SLHT on land purchased and owned on or after January 1, 1969 by a statute enacted in 1973.

The High Court dismissed their appeal, holding that although Article 39 of the Constitution banned retroactive criminal legislation, non-retroactivity was merely an interpretative principle in non-criminal fields. Retroactive legislation was not prohibited, it explained, by the Constitution itself. According to the Court, since the SLHT was introduced to correct the adverse effect of the 1969 legislation, there was reasonable ground to enact retroactive legislation. Therefore, the tax was not unconstitutional and invalid.

The logic of the decision is very difficult to understand. Although the SLHT Act imposed a tax on land purchased before its enactment,²⁹ it imposed the tax only on present and future land holdings. In that sense, it was not retroactive, and the decision should not have precedential value.

(c) Periodic Tax Cases

In the field of periodically levied taxes like individual and corporate income taxes, it often happens that amendments are made to the disadvantage of taxpayers during the tax period and applied from the beginning of the period. There are several cases in which the constitutionality of such legislation was disputed. In this paper, the following two cases will be introduced.

(i) Local Health Insurance Tax of Hamamatsu City Case

Decision of the Shizuoka District Court of October 27, 1972;
Administrative Cases Reporter, vol.23, no.10-11, p.774

²⁹ Since January 1, 1969.

Under the local health insurance system, health care expenses are financed by either the local health insurance tax or the local health insurance premium. Both the tax and the premium are imposed and collected for a fiscal year (April 1 to March 31) on a monthly installment basis (except September and October). Hamamatsu City was one of the local communities that adopted the local health insurance premium system. It is the consensus among constitutional law and tax law scholars that for the interpretation of Article 84 of the Constitution, the term “tax” also includes coerced burdens like local health insurance premiums. Hamamatsu City amended its National Health Insurance Ordinance in September 1968. This amendment was to be applied retroactively from the beginning of the period. Since it substantially increased the amount of premium to be paid by high income residents, some of them brought suit in the Shizuoka District Court. They claimed that because the increases in the premiums applied to past months, the amendment was void as unconstitutionally retroactive legislation.

The District Court elaborately examined why an amendment during the period was necessary. According to the Court, since the amount of the insurance to be paid to insured city residents and the standard price of the medicines covered by the health care increased since January of 1968, it was already predictable in 1967 that the health insurance premiums would substantially increase in 1968. A further factor in deciding the amount of premium for each resident was the amount of his or her local income tax which usually becomes final only in June. For these reasons, as in previous years, the ordinance was amended and the amendment was publicly announced in September. Based on this amendment, the standards for calculating the amount of the premium for 1968 were fixed in October. Then, the amount of the premium to be paid by each resident was decided in November.

On these findings, the Court held that for the technical reasons given above, it was unavoidable and predictable that the ordinance would be amended during the period and applied to the beginning of the period. Even if this constituted retroactive legislation, it did not seriously infringe the right to property guaranteed by the Constitution, and did not violate the principle of non-retroactivity of tax legislation.

For these reasons, the Shizuoka District Court dismissed the plaintiffs' claims, and held that the application of the ordinance amendment to the entire period was both unavoidable and understandable.

(ii) Real Estate Capital Loss Deduction Case

Decision of September 22, 2011, Supreme Court Civil Cases Reporter, vol.65, no.6, p.2756³⁰

2nd Instance Court: Decision of the Tokyo High Court of December 4, 2008, Supreme Court Civil Cases Reporter, vol.65, no.6, p.2891

1st Instance Court: Decision of the Chiba District Court of May 16, 2008, Supreme Court Civil Cases Reporter, vol.65, no.6, p.2869

This case concerns the 2004 amendments to the Income Tax Act. These revisions were introduced in the legislature in February of 2004, passed in late March, and promulgated immediately. Prior to the amendments, a long-term capital loss from the sale or exchange of real estate could be netted against other income. After the amendment, long-term real-estate capital gains were subject to tax at a lower rate than before, but losses could no longer be deducted from other categories of income. They could only be deducted from long-term real-estate capital gains income. Crucial to the case, the amendment applied retroactively to all transactions occurring after January 1, 2004.

The plaintiff had contracted to sell his land on January 30, 2004. He had owned the land since 1993, but transferred it to his buyer on March 1, 2004. Although the sale generated a capital loss for him, the tax office director cited the 2004 amendment to refuse to let him deduct the loss against other income. The plaintiff sued in Chiba District Court to vacate the decision, but the District Court denied his claim, and the Tokyo High Court affirmed. He appealed to the Supreme Court, but it affirmed as well. The Supreme Court explained as follows:

- (A) Article 84 of the Constitution requires the government to specify the preconditions for taxation clearly by statute. This rule ensures the legal stability of taxation.
- (B) When a statute changes the content of a legally defined set of property rights, the change can have an effect on legal stability. Whether the change is constitutional depends on the following considerations:
 - ① the nature of the property right in question;
 - ② the extent to which the statute changes that property right;
 - ③ the nature of the public interest furthered by the statute;

and on whether, considering these factors, the statutory change constitutes a

³⁰ As the same opinion on the same issue of the Supreme Court, cf. Decision of the Supreme Court of September 30, 2011, Hanreijiho, no.2132, p.39.

rational limit on the property right in question.

- (C) In the present case, the statute was amended during the course of the calendar year, but made retroactively effective to the beginning of the year. Whether that retroactive application violates Article 84 of the Constitution turns on considerations (B)① through ③ above.
- (D) The legislature passed the amendment in question to stop the steady fall in real estate prices by stopping panic-induced sales.
- (F) The effective date of the statute was only 3 months before its passage.

Given these factors, the Court found the retroactive application a rational exception to the general ban on retroactive tax legislation. Accordingly, it held that the application did not violate Article 84 of the Constitution.

One could interpret this decision as paralleling Article 29 of the Constitution. Article 29(b) limits property rights by reference to the public welfare; this opinion similarly limits the Article 84 ban on retroactive legislation by reference to policy considerations. The parallel, however, is problematic. Article 29(b) explicitly states that "[p]roperty rights shall be defined by law, in conformity with the public welfare." Article 84 includes no such reference to the "public welfare."

4. Principle of Legality

Because tax law is mandatory law, it gives the tax office little discretion. Provided the requisites to tax liability are satisfied, the office may not reduce or eliminate a taxpayer's liability. Neither may it opt not to collect any liability. Instead, it must levy and collect the amount of taxes specified by statute.

In Germany, this rule is known as the principle of legality (*Legalitätsprinzip*). In Japan, the courts have applied the principle consistently since the period before the war. The principle does not just reduce the unfairness that might otherwise shape the enforcement of the tax law. It helps prevent variations in taxpayer treatment that might otherwise render the equity of the tax burden hard to maintain.³¹

Accordingly, the government may not reduce a taxpayer's liability, eliminate his liability, or excuse his non-payment. Neither may it enter into settlements or agreements about the content of the tax liability, or the timing or method of tax collection (though settlement is possible if a statute clearly specifies the necessary

³¹ On this subject, cf, *Hiroshi Kaneko*, *Tax Law* (20th rev. ed. (2015)), p.81 et seq.

detail). Such private agreements are illegal, void, and unenforceable.³²

In fact, of course, the tax office and taxpayers sometimes reach agreements that strongly resemble settlements. They do so for the convenience of the parties and the efficient enforcement of the tax regime. Formally, however, these are not agreements that have a straightforward legal consequence. Rather, the agreements nominally have legal import only because the discussion between the office and the taxpayer affected the decision that the office reached about the facts behind the taxpayer's tax liability.

Note the following three permutations to this principle of legality. First, the tax office is bound by precedent. If the case law is advantageous to the taxpayer (if it reduces or exempts his taxable income, for example), the office must follow the precedent.³³ Second, the tax office is bound by its own general practice. If it broadly applies interpretations or procedures that are advantageous to taxpayers (and adopted no measures limiting those interpretations or procedures), it cannot arbitrarily refuse to apply them to a given taxpayer. Even without any case law on point, to apply the interpretations or procedures broadly but then to refuse to apply them to a given taxpayer would violate the principle of equal treatment.³⁴ Third, the principle of legality is limited by general principles of good faith and estoppel.³⁵

5. The Principle of Due Process in Taxation

To improve tax procedures is one of the most important functions of the rule of law in taxation.

(1) In considering the procedures that apply to tax assessment, bear in mind the peculiar role of the "blue return" system. Blue returns date from the 1949 Shoup Recommendations. The legislature adopted the recommendations, and introduced the blue returns in 1950.

The Shoup Mission envisioned the blue return system as a way to accustom small firms to keeping business records and filing returns. To file a blue return, taxpayers must keep books and records that met standards set by the Ministry of Finance. If they follow these standards, the government then grants them preferential tax treatments. These preferences include certain procedural rights. The government,

³² Decision of the Fukuoka District Court of April 18, 1950, Administrative Cases Reporter, vol.1, no.4, p.581. Cf, Decision of the Supreme Court of September 2, 1974, Supreme Court Civil Cases Reporter, vol.28, no.6, P.1033.

³³ *Hiroshi Kaneko*, Tax Law (20th rev. ed. (2015)), p.107.

³⁴ Id. P.91.

³⁵ Id. P.132.

for example, may reassess a blue-return taxpayers' liability only after it actually reviews the taxpayers' books and records. It may reassess that liability only if it explains to the taxpayer the reasons for the reassessment (Individual Income Tax Act § 155②, Corporate Income Tax Act §121, §130②).

The Supreme Court has interpreted strictly the requirement that the government explain the reasons for any reassessment. The leading case in question is the decision of May 31, 1963:³⁶

“The law requires that administrative dispositions give the reasons for the decision. In general, this is to help insure the prudence and rationality of the decision, and to suppress its arbitrariness. Additionally, by requiring that the government communicate the reasons for the disposition to the party, the law facilitates the filing an objection. Should an administrative disposition lack those reasons, the disposition itself is void.

This discussion leaves open the question of how fully a disposition should detail the government's reasons. The answer depends on the nature of the disposition, and the import and purpose of the statute providing for the disposition and the disclosure of the reasons for it. Article 45① of the Income Tax Act guarantees that income on a return may not be recalculated without regard to the proper entries in the legally required books. Accordingly, the reasons required by Article 45② are reasons for which the government must provide evidence with credibility greater than that of the taxpayer's books. With that evidence, the government must then make clear the actual basis for its decision.

In the case at hand, ... the taxpayer cannot determine (from the reasons [the government gave]) which of his accounting entries reflected how much leakage. He cannot determine the basis for the amounts [asserted by the tax office]. He cannot determine how the investigators arrived at the profit rate that they did. He cannot determine why the amounts based on that profit rate are correct. Given these inadequacies, we cannot find that the reassessment disposition meets the reason-disclosure requirement given in Art. 45 (2) of the Income Tax Act.”

³⁶ Supreme Court Civil Cases Reporter, vol.17, no.4, P.617.

The Supreme Court decision of April 23, 1985 further provides:³⁷

“[S]ometimes the tax office will issue a reassessment disposition without actually disputing any entries in the taxpayer’s books. Because such a reassessment disposition does not contest the taxpayer’s entries, the tax office does not introduce evidence with credibility greater than the taxpayer’s books. The office must, however, give reasons for its reassessment disposition sufficient to prevent arbitrary government action and to facilitate the taxpayer’s petition for review. They should be full enough to enable others to check the process by which it arrived at its reassessment disposition.”

However, the law did not require the tax office to disclose its reasons in determination dispositions involving blue-return taxpayers. Neither did it require the office to disclose its reasons in either reassessment dispositions or determination dispositions involving non-blue-return taxpayers.

Enacted in 1993, the Administrative Procedure Act required administrative agencies to give reasons when they issued denial dispositions of applications (e.g., an application for a business permit), or disadvantageous dispositions (Administrative Procedure Act, Arts. 8, 14). Tax disputes, however, Act Regarding General Rules for National Taxes (General Rules Act, hereafter) treated separately. Because of the large number of tax-related dispositions, the General Rules Act did not require reasons in all such dispositions. Instead, it exempted tax dispositions from the general requirement of stated reasons (General Rules Act, Art. 74-2(a)).

Over time, the demand for due process grew, and in 2011 General Rules Act was amended to require stated reasons -- both in denials of applications, and in disadvantageous dispositions (Art. 74-14(a) (parenthetical)). The government must now give reasons for determination dispositions involving blue return taxpayers, and for both determination and reassessment determinations involving all other taxpayers.

(2) In Japan, the procedures are not yet fully specified for administrative investigations (audits, inspections). Even the Administrative Procedure Act lacks such provisions. With respect to the field of tax as well, the various tax statutes had merely provided that the tax office may question taxpayers or inspect books and records as necessary for reassessments or determinations (e.g., the Income Tax Act, Art. 234, prior to amendment in 2011). The law did not require prior notice of the time, place, or

³⁷ Supreme Court Civil Cases Reporter, vol.39, no.3, P.85.

content of the investigations, or the reasons for the investigations. However, the 2011 amendment to the General Rules Act now requires prior notice. For a tax investigation, the tax office must notify the taxpayer of the beginning time and place of the investigation. It must detail the purpose of the investigation, the tax items involved, the expected length of time, and the objects to be investigated.

When the investigation is complete: (i) if reassessment or a determination is not appropriate, the director of the tax office must notify the taxpayer in writing that neither a reassessment nor a determination is appropriate (General Rules Act, Art. 74-11(a)); (ii) if reassessment or a determination is indeed appropriate, the official in charge must explain to the taxpayer the results of the investigation (the reasons for the reassessment or determination, and the amounts involved) (*id.*, Art. 74-11(b)); (iii) when the official gives this explanation, he must explain that a taxpayer who filed a return may not file an objection, but may demand a reassessment, and must provide written statement to this effect (*id.*, Art. 74-11(c)).

Through these changes to the General Rules Act, the systematization and reform of tax procedures has progressed. The guarantees of due process in tax -- even if not yet entirely adequate -- have greatly increased.

6. Principle of Judicial Protection of Taxpayer Rights

The guarantee of taxpayer rights in the courts is an essential element of rule of law in taxation.³⁸ The Meiji Constitution provided for Administrative Court outside the scope of the regular courts, and placed jurisdiction over tax litigation with the Administrative Court. There were three problems. First, it was located only in Tokyo. Second, it was a sole instance court. Therefore, there was no possibility of appeal. Third, the majority of judges were former government officials. For the protection of the taxpayers' rights, it was inadequate.

By contrast, the current Constitution places the jurisdiction over all disputes with the ordinary courts (headed by the Supreme Court) (Art. 76(a)). It prohibits all special courts (Art. 76(b)), abolishes the administrative court system, and moves all litigation involving administrative disputes within the ambit of the general court system. Reflecting this mandate, the Courts Act (Art. 3) specifies that the general courts adjudicate all legal disputes. Should a taxpayer receive an illegal tax disposition, he may sue in an ordinary court, and receive its protection.

Administrative cases, however, often require different procedures from

³⁸ cf. *Hiroshi Kaneko*, *Tax Law* (20th rev. ed. (2015)), p.941.

standard civil disputes. Reflecting this need, the Administrative Case Litigation Act specifies distinct procedures that apply to these administrative cases -- unless other statutes provide to the contrary (*id.*, Art. 1). As one type of administrative dispute, tax cases are governed by this statute except where the tax statutes or orders specify otherwise.

The Administrative Case Litigation Act generally abolished the principle of exhaustion of administrative remedies. Instead, it gives parties the right to choose whether to sue immediately, or first to pursue administrative options instead (Art. 8(a)). This rule does not apply to tax disputes, however. Instead, the General Rules Act (Art. 115(a)), the Customs Act (Art. 93), and the Local Tax Act (Art. 19-12) adopt the principle of exhaustion of administrative remedies: before a taxpayer may contest a tax determination in court, he must first pursue the administrative process.

To contest a disposition of a national tax, a taxpayer needed to take two administrative steps: file an objection with the director, and appeal to the National Tax Tribunal (organizationally located within the National Tax Agency; General Rules Act, Art. 115(a)). To contest a disposition of a local tax, he needs to obtain a determination regarding his objection or a decision of upper rank agency regarding his appeal (Local Tax Act, Art. 19, Administrative appeal Act, Art. 4-1, 4-4).

Two reasons lie behind this use of the exhaustion of administrative remedies principle in tax cases. First, disputes about the assessment and collection of taxes are many. In order to prevent tax disputes from overwhelming the courts, it was necessary to route as many cases as possible to administrative tribunals. Second, tax disputes require specialized expertise. Because they often involve the interpretation of complex tax provisions and the determination of difficult facts, they require both specialized and technical knowledge. At the very least, the administrative process can accomplish a screening function: it can provide a close investigation and clarify the points in dispute.

Nevertheless, to require taxpayers to pursue two administrative proceedings before filing suit contravened the goal of providing them with simple and quick remedies. Accordingly, the June 2014 amendment to the General Rules Act eliminated the requirement that taxpayers file objections with the tax office. They may instead move directly to adjudicative proceedings at the National Tax Tribunal.

Although this Tribunal is organizationally a part of the National Tax Agency, it is granted independence in the exercise of its powers. It has its headquarters in Tokyo, but maintains branches in each of the eleven locations where the National Tax Agency has a Regional Office. Branches (like Osaka Branch) that handle many disputes

maintain sub-branches as well.

Taxpayers bring their appeals before the branch or sub-branch of the National Tax Tribunal holding jurisdiction over the tax office with which they have a dispute. Each case is handled by a panel of three appeals judges. At the time of the initial establishment of the Tribunal in 1970, the Chief Judge was a former judge of High Court, the posts of chief judge of the key Branches were given to judges seconded from the general courts, or to prosecutors seconded from the national prosecutorial corps. The other tribunal judges were selected from among employees of the National Tax Agency. In order to maintain the Tribunal's neutrality and to build taxpayer confidence in the system, the government has increasingly appointed men and women other than tax agency employees. They have included lawyers, tax practitioners, accountants, and scholars, as well as the general judges and prosecutors. Under the current plan, half of the tribunal judges (50 of the 99) will come from backgrounds other than the National Tax Agency by 2025.

The proceedings of the tribunal are generally conducted through written filings. However, when a taxpayer asks for a chance to speak, the tribunal is obligated to give him an opportunity to present his case in person. The tribunals do not make use of the adversary system, though I personally believe that taxpayers should be entitled to choose adversary procedures.

In order to prevent surprise attacks, the office is not allowed to change the basis for any assessment. Should it become clear in the course of a tribunal proceeding that the factual basis for the original disposition was false, for example, the tax office may not introduce other facts to justify its assessment. This rule is known as the "principle of no change of original issue."

Final Remarks

In II. above, some important cases concerning the principle of statute-based taxation (rule of law) were introduced. Based on this principle, the claims of taxpayers were sustained in many of these cases. It could be said that the principle of statute-based taxation (rule of law) has been established gradually in the case law.

In this as in other matters, the interaction between scholarly opinion and court decisions has worked for the development of this principle, and both scholarly opinion and court decisions have helped to improve tax legislation and tax administration.

However, only a part of administrative activity is actually checked by the courts. Accordingly, the principle of statute-based taxation (rule of law) is raised as an issue in

courts only for small part of tax legislation and administration. Therefore, the gradual establishment of the principle in the case law does not mean that the principle is established sufficiently in actual legislation and administration.

As mentioned above, the principle of statute-based taxation serves two different but related values: first, the traditional constitutional value of “no taxation without representation”; and second, predictability and legal stability (certainty) in taxation. In other words, the first value is expected to work toward the realization of democracy in taxation, and the second value is expected to protect people from arbitrary taxation. Both values have been historically important and will continue to be important in the future, too.

Concerning the second value (maintaining predictability and legal stability in taxation), I would like to point out the importance of the following two problems.

First, both court decisions and academic opinions in Japan take the position that in principle the provisions of tax law should be rigidly and strictly interpreted. When the provisions of tax law use the same concepts that are used in the statutes concerning private transactions (Civil Code, Commercial Code, Corporation Act, etc.), in principle these concepts should be interpreted in the same meaning as in those private transactions statutes. This way of interpretation serves to keep predictability and legal stability in taxation.

Second, the advance ruling system used in the U.S. and some other countries is useful and convenient to keep predictability and legal stability for taxpayers. Through the system, taxpayers can learn the views of tax agencies in advance regarding the tax effects of the transactions they are planning to do. I proposed in the mid-1960s that this system be adopted in Japan. Japan delayed in adopting it for various reasons, but finally adopted it in 2004. The Japanese system is similar to the U.S. system.

Finally, for the further development and establishment of rule of law in taxation, it is indispensable to emphasize the importance of rule of law. Both tax legislation and tax administration would be gradually improved by an emphasis on the importance of rule of law in taxation. Therefore, it should be a mission of law scholars to emphasize the importance of rule of law in taxation. If they continue to do so, it could be expected that rule of law in taxation would also continue to develop step by step.