

Implementing Structural Reforms in Abenomics: How to Reduce the Cost of Doing Business in Japan

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ABSTRACT

Improving the environment for business is an important part of the growth strategy of Abenomics. As the KPI (Key Performance Indicator) for this effort, the Abe Administration aims to improve Japan's rank in the World Bank Doing Business Ranking from the current #15 among high-income OECD countries to one of the top three. This paper clarifies what it takes for Japan to be among top three countries in terms of ease of doing business. By looking at details of the World Bank Doing Business ranking, we identify various reforms that Japan could implement to improve the ranking. Then, we classify the reforms into four groups depending on whether the reform requires legal changes and whether the reform is likely to face strong political resistance. By just doing the reforms that do not require legal changes and are not likely to face strong political opposition, Japan can improve the ranking to 9th. To be in the top 3, Japan would need to implement all the reforms except for those that require changing the laws *and* are likely to face strong political resistance, even under the unrealistic assumption that the other countries do not reduce the cost of doing business. Thus, in order to be one of the top three countries among OECD countries in terms of ease of doing business, Japan would most likely need to carry out all the reforms identified in this paper.

1. Introduction

Abenomics seems to be working so far. Since the Liberal Democratic Party (LDP) came back to power in December 2012 and Prime Minister Shinzo Abe announced the new economic policy dubbed “Abenomics,” the economic conditions in Japan have improved. More aggressive monetary policy introduced by the Bank of Japan under the leadership of Governor Haruhiko Kuroda seems to be ending the chronic deflation. The GDP growth has been substantially higher than it was expected before the start of Abe administration.¹ Even after the consumption tax increase on April 1, 2014, the economic slowdown seems to have been well within the expected range.

Can Abenomics sustain the early apparent success and pull the Japanese economy out of the low growth that has characterized most of the last 20 years? The answer hinges on the success of the growth strategy part of Abenomics, which is referred to as the third arrow. Even if the first two arrows of Abenomics (bold monetary policy and flexible fiscal policy) turn out to be successful, the best they can do is to fix the demand shortage and eliminate the output gap. The growth strategy is supposed to address issues for Japan’s long-term growth. In order for Japan to escape the long-term stagnation and achieve a higher potential growth, the growth strategy part of Abenomics also needs to be successful.

The growth strategy is not a new invention of the Abe administration. Two administrations (led by the Democratic Party of Japan (DPJ)) that immediately preceded the Abe administration also formulated their own growth strategies. In both cases, the prime ministers were forced out before the growth strategy was fully implemented.

There is one thing new about the growth strategy in Abenomics: the planned use of Key Performance Indicator (KPI). KPIs are assigned to policy goals in the growth strategy and are used to measure the progress. Although many KPIs that have been proposed for Abe’s growth strategy are vague as Hoshi (2014) points out, there are a few that are clearly specified. The updated growth strategy that was approved by the Cabinet in June 2014 includes the discussion on the current status of KPIs.

This paper takes up one of the clearly specified KPI, examines what it would take for Japan to achieve the KPI, and proposes a path to accomplish the goal. The KPI that we focus on is the goal of improving Japan’s ranking in the World Bank Doing Business Ranking to increase “Japan’s international competitiveness.” The KPI states “Japan will be one of the top three countries (currently 15th) in the business environment ranking for the developed countries reported by the World Bank in “Doing Business Report” by 2020.”

Focusing on the business environment makes sense since there is a growing consensus in economic research that the quality of business regulation and the institutions that enforce it are a major determinant of employment creation, private sector development, and economic

¹See Buiter and Rahbari (2013), Hausman and Wieland (2014), and Hoshi (2014) for more on Abenomics and its evaluations.

prosperity.² For example, Haidar (2012) examined the link between regulatory reforms and economic growth in 172 countries using World Bank Doing Business data, and found that each regulatory reform is associated with a 0.15 percent increase in the real GDP growth rate on average. For Japan, Hoshi and Kashyap (2012) list reduction of cost of doing business as one of the important policy options to restart the growth.

This paper clarifies how much reform Japan needs to make to move from 15th (among 31 high income OECD economies) to top three and presents a strategy to get there. To do this, we use the information in the 2014 Doing Business Report. Although the KPI is based on the 2013 Report, Japan is ranked 15th among 31 high income OECD economies in both reports, so the use of 2014 Report would not create any substantial problems.

The paper is organized as follows. The next section studies where Japan is ranked in the 2014 Report in each of the ten areas that the World Bank Doing Business Project looks at to come up with the ranking. We also identify potential regulatory reforms in each area that would improve Japan's ranking. Section 3 then examines the identified regulatory reforms from two perspectives: whether the reform requires any legal changes and whether the reform is likely to face strong political resistance. The reforms that are primarily administrative and are not likely to be political can be accomplished quickly. The reforms that require changes to prevailing laws and/or are likely to be political would take more time. We consider a sequencing of reforms that starts out with the simple administrative reforms followed by more in-depth reforms and examine how far Japan needs to go to move from 15th to 3rd in the World Bank Doing Business Ranking. Section 4 concludes.

2. Japan in the World Bank Doing Business Ranking

Japan is ranked 27th overall among the 189 economies covered by the World Bank 2014 Doing Business Project, but 15th out of the 31 high income OECD economies.³ The ranking is compiled by the World Bank every year by looking at ten areas of doing business, many of which are critically influenced by government regulations. Japan is ahead of other countries in some areas such as getting credit, protecting investors, trading across borders, and resolving insolvency. As shown in Table 1, Japan is ranked 9th, 8th, 14th, and 1st among OECD economies respectively in these areas.⁴ Japan can do better, however, in the other areas. In the ease of starting a business, dealing with licenses, registering property, and paying taxes, Japan is ranked 28th, 21st, 22nd, and 31st among the 31 OECD economies respectively. This section reviews Japan's ranking in each of the ten areas and identifies some regulatory reforms that Japan can implement to improve its ranking.

2-1. Starting a business

²See Blanchard and Portugal (1998), Holmes (1998), Besley and Burgess (2004), Alesina et al. (2005), Klapper et al. (2006), Ciccone and Papaionnou (2007), Dabla-Norris et al. (2008), Klapper and Love (2010), and Haidar (2012) among others

³World Bank Doing Business 2014 Report.

⁴Throughout the paper, we refer to OECD as the set of 31 OECD high income countries, not to the set of 34 OECD members. The latter (34 member) group includes Chile, Mexico, and Turkey.

Japan currently ranks 28th out of the 31 OECD economies on the ease of starting a business. It is estimated to cost 7.5% of Japan's income per capita (of 2012) to formally start a business in Tokyo. The process takes 8 procedures and requires 22 days in Japan. In comparison, an entrepreneur can start a business by following just one procedure, in a half day, and at a cost of 0.3% of income per capita in New Zealand. Similarly, starting a business requires only 3 procedures and no more than 4 days in Australia. It costs only 0.4% of income per capita to start a business in Canada.

There are several reforms that Japan can implement to reduce the number of steps, the monetary cost, and the time to start a business in Japan. Here we discuss the following four reforms.

- *Eliminate the requirement for a company seal (reform 2.1.1)*
- *Make business registration administrative rather than judicial (reform 2.1.2)*
- *Create one-stop shop for business registration (reform 2.1.3)*
- *Cut registration fees (reform 2.1.4)*

Eliminate the requirement for a company seal: Currently, an entrepreneur is required to make a company seal and register it. These two procedures take about 4 days. The company seal is required, per Article 20 of the Commercial Registration Act. The associated fee is about ¥10,000 for machine-carved seal or ¥20,000 for hand-carved seal. The entrepreneur or a company representative must register the company seal and obtain the certificate of seal registration from the Ward office in person. The certificate then must be submitted to the Legal Affairs Bureau at the Ministry of Justice. The fee is approximately ¥400 per certificate of seal registration but varies from ward to ward. The requirement is a legacy of the old business practice where a seal symbolized the legal identity of a business and authenticated all its contracts.

Make business registration administrative rather than judicial: To apply for registration, an entrepreneur submits a duly completed application form, along with supporting documents including the certificate of seal registration and the Articles of Incorporation to the Legal Affairs Bureau headquarter or any of its branch offices in major cities (Tokyo, Yokohama, Osaka, Nagoya, Kobe, and Fukuoka). Once the filed documents are reviewed and approved, the company applies for the issuance of a company registration certificate. Normally, a judicial scrivener completes the registration on behalf of the company. The whole process takes one to three weeks in Japan. The 2004 amendment to the Commercial Registration Regulations has made it possible for entrepreneurs to submit company registration applications online, but the time this legal process takes has not been shortened.

Japan can reduce the time for business registration by making it a simple administrative process rather than judicial process. This changeover is straightforward and has been done in many countries less developed than Japan, including Serbia, Uganda, Bulgaria, and Honduras.

Create one-stop shop for business registration: Currently, the eight procedures that must be completed to start a business in Japan require an entrepreneur to visit almost as many regulators

including the Ward Office (to obtain the certificate of seal registration), Ministry of Justice, District Tax Office, Municipality, Labor Standards Inspection Office, Japan Pension Service, and Public Employment Security Office. Cumbersome registration procedures mean more hassle for entrepreneurs. Creating one-stop shops for company registration has been a popular reform over the last decade in many countries. For example, Portugal combined company, tax and social security registrations in one building. A one-stop shop in Tokyo would allow entrepreneurs in Japan to register with all the above agencies in a single visit and can open their businesses faster.

Cut registration fees: It currently costs 0.7% of the official stated capital or ¥ 60,000, whichever is higher, to register the company at the Legal Affairs Bureau of the Ministry of Justice in Japan. This amount (¥60,000) is equivalent to 7% of Japan's income per capita. The cost in Denmark is only 0.2% of its income per capita. Registration fees account for the bulk of the direct monetary cost to start a business in Japan. By reducing registration fees to the level of Denmark (0.2% of income per capita), Japan can substantially cut the cost to start a business.

2-2. Dealing with construction permits

Japan stands at 21st out of 31 OECD economies on the ease of dealing with construction permits. This indicator measures what it takes to comply with formalities to build a warehouse in Japan. These formalities currently require 14 procedures compared to 7 in Sweden, 193 days compared to 29 days in South Korea, and direct monetary cost of 28.1% of income per capita compared to 13.3% in Australia.⁵ Instead of making the process cheaper, Japan made dealing with construction permits more costly by increasing inspection fees in 2012.

It would not be a good idea to do away with construction permits completely because sound regulation of construction helps protect the public from faulty building practices. Moreover, enhancing public safety, well-functioning building permit and inspection system can also strengthen property rights and contribute to the process of capital formation⁶.

Japan, however, can reduce the cost for entrepreneurs to deal with construction permits without compromising building safety. The measures that are discussed below are:

- *reduce number of permits (reform 2.2.1)*
- *introduce statutory time limits for issuing a permit (reform 2.2.2)*
- *limit inspections (reform 2.2.3)*

Reduce the number of procedures: A company in Japan must complete 14 steps to legally build a warehouse, according to the World Bank Doing Business database through information collected from experts in construction licensing, including architects, civil engineers, construction lawyers, construction firms, utility service providers and public officials who deal with building regulations. These procedures include acquiring permits/consents from local

⁵ Sweden, South Korea, and Australia stand at 6th, 5th, and 2nd respectively out of 31 OECD economies on the ease of dealing with construction permits.

⁶ World Bank (2013)

authority, neighborhood, Building Department of Government of Tokyo, Labor Control Office, Japan Building Center, and Land and Building Registry.

Some of these procedures are redundant and can be merged with other ones. For example, currently the builder needs two separate procedures to receive intermediate and final inspections from Japan Building Center and another procedure to obtain completion certificate.

Japan can benefit from the experience of various OECD countries that reduced the number of construction licenses. In Germany some simple construction projects no longer require a permit. Instead, the builder only notifies the municipality when construction starts. Inspectors show up at the site once the project has begun. After this reform the time to comply with licensing and permit requirements fell from 165 days to 133. In France the number of licenses required for construction projects was reduced from 11 to 9. In Sweden, only 9 procedures are required, too. Elsewhere in Europe, Spain no longer requires an installation license on top of the building license, cutting the number of procedures by one.

Introduce statutory time limits for issuing a permit: The procedures to get approvals from the Building Department of Government of Tokyo and Labor Central Office account for the bulk of time required -- 130 out of 193 days -- to deal with construction permits. Two other procedures to get approvals from Japan Building Center and Water and Sewage Services account for additional 45 days. Japan can reduce the number of days to deal with construction permits by introducing statutory time limits.

In France, the average amount of time to get a construction permit was reduced by one month by requiring the building inspectorate to visit and issue a declaration of work completion within 3 months. In addition, the government can introduce “silence is consent” rules for issuing building licenses. For example, Spain set the maximum time for approval at 90 days and adopted the “silence is consent” rule at the same time. Similarly, the Netherlands introduced a 45-day limit.

Limit inspections: Another reform that can smooth the process is adjusting licenses and inspections to the size and nature of the project. Smaller projects could receive less scrutiny, lowering compliance costs and allowing regulators to focus their energy on more complex projects. Korea implemented such reform in 2006. It exempted small construction projects from the requirement to apply for an advance building permit.

2-3. Getting electricity

Japan currently ranks 10th on the Ease of Getting Electricity indicator. This indicator tracks the number of procedures, the time, and the direct monetary cost necessary for a business to obtain a permanent electricity connection for a newly constructed warehouse. Getting access to electricity to a warehouse in Japan requires 3 procedures, takes 105 days although it costs a negligible amount of money. It takes only 17, 18, and 22 days in Germany, South Korea, and Iceland, respectively.⁷

⁷ Germany, South Korea, and Iceland currently rank 3rd, 2nd, and 1st, respectively, on the Ease of Getting Electricity indicator.

While Japan performs well on the number of procedures and the direct monetary cost, it can implement the following reform to improve its ranking:

- *Improve process efficiency (reform 2.3.1)*

Improve process efficiency: Japan can reduce the time between submitting application to TEPCO and getting connection works. After an initial contact with TEPCO on construction date and effective date of contract, it currently takes 93 days before electricity connection works start. After an average of 93 days of waiting, TEPCO takes 11 more days to carry out connection works and install a meter.⁸

Examples from the rest of the world show that it is possible to increase the efficiency of utilities' internal processes and reduce the electricity connection delays. Malaysia, Mexico, and Turkey made getting electricity easier by improving communications with contractors, introducing electronic document management systems and increasing staff and resources for inspections. In Burundi the electricity utility Regideso ended its monopoly on the sale of transformers and other equipment needed for electricity connections. Since June 2012 the change has decreased the time to obtain a connection by 30 days because customers can now import materials instead of buying them from Regideso if the materials are not in the company's stock. The utility also opened a center that combines all the internal services of the utility involving new connections. Mexico's electricity utility, Comisión Federal de Electricidad, streamlined the process for obtaining electricity, offered training to contractors and implemented a geographic information system (GIS) that maps the electricity network. This commitment has paid off: the time to obtain a new electricity connection in Mexico City dropped from 291 days in 2009 to 85 in 2013.

2-4. Registering property

Japan is currently ranked 22nd on the ease of registering property. Doing Business records the full sequence of procedures necessary for a business to purchase property from another business and transfer the property title to the buyer's name. The transaction is considered complete when it is opposable to third parties and when the buyer can use the property, use it as collateral for a bank loan or resell it.

Registering property in Tokyo requires 6 procedures, takes 13 days and costs 5.8% of the property value. More than 30 countries made it easier to register property since 2006. Japan was not one of them, although its property registration process is relatively complicated compared to other OECD countries. It is easier to register property in New Zealand than anywhere else in the world. The entire process can be completed in 2 online procedures at a monetary cost of 0.1% of the property value. Lawyers certify land transfer documents for their clients and submit them electronically for registration. Confirmation is returned within minutes. In general, the cost of

⁸Since the data were collected in 2012 and 2013, one might wonder if the long delays in Japan may reflect TEPCO's troubles after its nuclear power plant accidents following the earthquake and Tsunami of March 2011. But it is not the case. The delay was already long before 2011. For example, in the 2010 ranking, the total number of days it typically took from application to the end of connection works were 105 days.

registering property is lower by 26% on average in common law compared with civil law countries, a result largely driven by differences in non-notary costs of registering property.⁹

To improve its ranking in this category, Japan can:

- *introduce fast-track procedures (reform 2.4.1)*
- *combine and eliminate some procedures (reform 2.4.2)*
- *lower registration fees (reform 2.4.3)*

Introduce fast-track procedures: An entrepreneur currently spends 7-10 days to file an application for registration at the Legal Affairs Bureau. The Legal Affairs Bureau registers the title under the name of the new owner. As registration is a requirement for perfection against third parties, reviewing the certified copy of the real property registry is generally sufficient for identifying any existing encumbrances over the real property. The parties may apply for registration by themselves. However, because of the complexity of filing, usually they retain a judicial scribe for registration.

The Legal Affairs Bureau may be in need of some structural reforms to reduce their respective delays but such reforms might require long-term efforts. In order to speed up registration in the meantime, the Legal Affairs Bureau could offer clients a choice of expedited procedures: pay a slightly higher fee and the registration is completed faster. It could offer expedited processing of 1-2 days, instead of waiting 7-10 days. Cases would be prioritized in a transparent manner, and those that prefer not to wait would be given an official way to speed up the process by 8-9 days in total. This type of scheme is offered in a number of countries around the world, from Singapore to Netherlands. Singapore introduced an online fast-track registration process for single transfers, enabling property transfers to be completed in one day. Simultaneously, the Legal Affairs Bureau can work on further reforms to reduce time for everyone – for example, by adopting shorter time-limits to process applications.

Combine and eliminate some procedures: Each party of the transaction must obtain a corporate registry certificate that has been issued within 3 months before the application. It can be obtained from a corporate registry office where the party is registered. The cost is ¥700 per copy (¥550 if obtained online). The seller also must obtain a certificate of its seal used for execution of the registration documents (issued within 3 months). It can be obtained from the Legal Affairs Bureau. The cost is ¥500 per copy (¥440 if obtained online). These two procedures can be combined, especially as the seller also needs to obtain yet another certificate of evaluation for property tax at a local tax office. Japan can also cut the requirement to obtain stamps for stamp duty at a post office. Instead, the payment, if needed, can be made at the Legal Affairs Bureau.

Lower registration fees: Currently, an entrepreneur in Tokyo must pay a registration and license tax of 1.75% of property value and a property acquisition tax of 4% of property value. The cost to register could be reduced significantly by replacing these taxes by a fixed fee. High percentage-based taxes may lead some entrepreneurs to resort to underreporting their property value to avoid paying the full amount or to avoid registration completely. As a result of such

⁹ Amin and Haidar (2012)

reform, Japan would be able to make the cost of registering property as low as 0.1% of property value, as in New Zealand, which is ranked 2nd in this category.

Many governments have reduced the cost of property registration by establishing a low fixed registration fee rather than charging entrepreneurs a percentage of the property value. In 2005, Slovakia abolished its 3% real estate transfer tax and set a low fixed fee for expedited registration at 8,000 Koruny (\$286). In 2007, Egypt and Poland adopted similar reforms. These reforms also ended up reducing fraud in reporting the value of property and increased tax revenues. Six months after Egypt replaced its 5.8% registration fee with a fixed fee of 2,000 Egyptian pounds (\$323), the revenues rose by 39%.¹⁰

2-5. Getting credit information

Two types of frameworks can facilitate access to credit and improve its allocation: credit information systems and laws on collateral and bankruptcy. Credit information systems enable lenders to view a potential borrower's financial history (positive or negative). And they permit borrowers to establish a good credit history that allows an easier access to credit. Sound collateral laws enable businesses to pledge their assets as security to raise funds. The past research found strong creditors' rights specified in collateral and bankruptcy laws are associated with higher ratios of private sector credit to GDP.¹¹

The World Bank Doing Business ease of getting credit index assesses the sharing of credit information and the legal rights of borrowers and lenders with respect to secured transactions using two indices. The depth of credit information index examines rules and practices affecting the coverage, scope and accessibility of credit information available through public credit registries and private credit bureaus. The strength of legal rights index measures whether certain features that facilitate lending exist within the collateral and bankruptcy laws of the country.

How well do the credit information system and laws on collateral and bankruptcy in Japan facilitate the access to credit? Japan has a full score of 6 (out of 6) on the depth of credit information index and a score of 7 (out of 10) on the strength of legal rights index. Higher scores indicate more credit information and stronger legal rights for borrowers and lenders. Japan is ranked 9th among OECD economies on the ease of getting credit.

To improve its ranking on the ease of getting credit indicator, Japan can (i) extend security right automatically to products, proceeds or replacements of the original and future assets after acquisition (*reform 2.5.1*), (ii) index the collateral registry by debtors' names (*reform 2.5.2*), and (iii) allow secured creditors to be paid first (before tax claims and employee claims) when a business is liquidated (*reform 2.5.3*). By completing these 3 reforms, Japan can jump to be the first among the OECD countries (and in the world) on the ease of getting credit indicator.

2-6. Protecting investors

¹⁰Haidar (2008)

¹¹Djankov et al (2007)

The “protecting investors” indicator measures the transparency of related-party transactions, liability for self-dealing, and shareholders’ ability to sue officers and directors for misconducts. Japan currently ranks 8th among the OECD countries on the strength of investor protection index. It scores 7/10 on the extent of disclosure index, 6/10 on the extent of director liability index, and 8/10 on the ease of shareholder suits index.

One of the most important potential problems in corporate governance is self-dealing: the use of corporate assets by company insiders for personal gain. Related-party transactions are the most common example. High ownership concentration and informal business relations can create the perfect environment for such transactions, which allow controlling shareholders to profit at the expense of the company’s financial health. Company assets may be sold at an excessively low price to controlling shareholders, assets may be bought at an inflated price from controlling shareholders, or company loans are given to controlling shareholders on terms far better than the arms-length offers.

Economies with strong protections of minority investors would have clear and detailed rules on disclosure and duties for corporate directors. They would also have well-functioning court system to allow minority shareholders to obtain judgments within reasonable time.

Empirical research shows that the level of investor protection matters for cross-country differences in income growth: countries with stronger protections tend to grow faster than those with poor investor protections.¹² Moreover, stricter regulation against self-dealing is associated with larger equity investment and less concentrated ownership.¹³ This is in line with the view that stronger legal protections make minority investors more confident about their investments and reduce the need for concentrated ownership to mitigate weaknesses in corporate governance.

To further strengthen investor protections, Japan could:

- *increase disclosure requirements (reform 2.6.1)*
- *make it easier to sue directors (reform 2.6.2)*
- *open company books for shareholder inspection (reform 2.6.3)*

Increase disclosure requirements: Japan currently scores 7/10 in the extent of disclosure requirements. By implementing the following three reforms, Japan can improve the score to perfect 10/10. First, Japan can require a resolution at both a board meeting and a general shareholders meeting to approve business transactions that entail a conflict of interest of a director and majority shareholders. Currently a resolution at the board level is sufficient. Second, a review by an external body for such transaction can be required before it takes place. Third, Japan can require immediate disclosure, to the public and/or shareholders, of transactions that entail a conflict of interest.

Increase directors’ liability: Japan currently scores 6/10 on the extent of director liability. Japan can improve the score to 10/10 by implementing the following three reforms. First, Japan can

¹²Haidar (2009)

¹³Djankov et al (2008)

give the judicial system the power to void a business transaction if the transaction is deemed unfair to minority shareholders or entails a conflict of interest. Second, directors can be required to pay the damages caused to the company and also repay the profit made from self-dealing. Third, a director at fault can be punished by fines and imprisonment.

Open company books for shareholder inspection: Japan already scores 8/10 on shareholder suits, but it can improve the score to perfect 10/10 by adopting the following two reforms to further improve the access by shareholder plaintiff to company books. First, it can allow the minority shareholders plaintiff to request categories of documents from the corporate defendant without identifying specific ones. Second, the plaintiff can be allowed to obtain any document that may lead to the discovery of relevant information, not only information that is already known to be relevant to the subject matter of the claim.

2-7. Paying taxes

The Doing Business paying taxes indicator measures the time and cost associated with paying all taxes and other mandatory payments as required by government. Japan is ranked 31 out of 31 in OECD, making this the lowest performing area for Japan. On average, a firm makes 14 tax payments a year, spends 330 hours a year preparing, filing, and paying taxes and pays 49.7% of profit as taxes.

Efficient tax administration can help encourage businesses to become formally registered thereby expanding the tax base and increase tax revenues. Administration that is unfair and capricious will bring the tax system into disrepute and weaken the legitimacy of government. Overly complicated tax systems are associated with high tax evasion. High tax compliance costs are associated with larger informal sectors, more corruption and less investment. Economies with simple, well-designed tax systems are able to help the growth of businesses and, ultimately, the growth of overall investment and employment.¹⁴

To improve its ranking on the ease of paying taxes, Japan can:

- *reduce number of payments (reform 2.7.1)*
- *reduce corporate profit tax rates (reform 2.7.2)*

Reduce number of payments: While a company needs to make 3 tax payments in Hong Kong, 4 in Sweden and Norway, and 5 in Singapore, it has to make 14 payments in Japan. In Norway, the 4 payments are corporate income tax, social security contribution, value added tax, and fuel tax. In addition to these 4 payments, a company in Tokyo must also pay inhabitants tax, a depreciable fixed assets tax, a fixed assets tax on land and building, employer paid employment and health insurance premia, real property acquisition tax (for building expansion), business premises tax (on floor space), stamp tax (on contracts for land sale and building expansion), registration and license tax, automobile tax, and automobile tonnage tax.

Multiple taxation, where the same tax base is subject to more than one tax treatments, appears to be making tax compliance cumbersome for taxpayers in Japan. Multiple taxation

¹⁴Djankov et al (2010)

increases the cost of doing business for firms because it increases the number of payments and compliance time. Different forms have to be filled out, often applying different methods for calculating the tax.

Consolidating taxes would be a worthwhile reform. Tax offices can then distribute the revenues among government agencies. Slovakia did just that: its single social contribution tax funds health insurance, sickness insurance, old age pensions, disability insurance, unemployment benefits, injury insurance, guarantee insurance and reserve fund contributions. In many countries social security agencies would be reluctant to part with their powers, especially if there is a chance that the central tax office will not give them their share of revenues. To gain their trust, a formulaic allocation of revenues can be introduced so that there is little room for discretion.

Fifty-five economies have one tax per tax base. This keeps things simple. Having more types of taxes requires more interactions between businesses and tax agencies. It also complicates tax compliance.

Businesses in Korea no longer need to calculate numerous taxes on the same base. Starting with the 2010 tax year, property taxes and city planning taxes are being merged with other taxes. And thanks to an effort aimed at unifying social security laws and administrations, businesses can now file and pay 4 labor taxes and contributions in a single payment. This freed them from the requirement to file additional returns and bear additional tax compliance costs.

Canada has harmonized and simplified its tax system. Beginning in the 2010 tax year, businesses are subject only to the federal harmonized sales tax, which replaced the former federal goods and services tax and provincial sales tax.

The time required to pay taxes estimates the number of hours it takes a typical company to gather data, analyze accounting information to highlight sensitive tax items, calculate tax liability, and submit payments. The process is estimated to take 330 hours in Japan but only 63 hours in Switzerland.¹⁵ By reducing the number of payments, Japan can also reduce the number of hours it takes a company to pay taxes.¹⁶

Reduce corporate profit tax rate: The total tax rate (as % of profit) is 24.3% in Canada and 25.7% in Ireland but 49.7% in Japan. While the marginal statutory corporate income tax rate is 6.6% in Canada and 12.3% in Ireland, it is 27.9% in Japan. And, the labor tax and contributions account for 12.9% in Canada, 12.1% in Ireland, and 17.9% in Japan. Japan could benefit from reducing the total tax rate.

Reduction of the corporate tax rate is one of the reforms that the Abe administration specified in the updated growth strategy in June 2014. The government aims to reduce the effective tax rate by more than 5% in several years and by more than 10% in the long run, but the concrete timeline for the reform is not specified, yet.

¹⁵ For comparability purpose, the Doing Business Project takes a standard case/company in each country for each area. In estimating the time it takes to pay taxes, the standardized company is assumed to have a turnover of 1050 times income per capita.

¹⁶ In section 3 below, we assume Japan reduces number of payments to 4 and hours to 60.

2-8. Trading across borders

Japan is ranked 14th out of 31. The Doing Business trading across borders indicator measures the time and cost associated with exporting and importing a standardized cargo of goods by sea transport. The time and cost necessary to complete every official procedure for exporting and importing the goods are recorded. All documents needed by the trader to export or import the goods across the border are also recorded. In France and Ireland, only two documents (the bill of lading and customs declaration) are required to export or import. But, in Japan, one more document (the commercial invoice) is required to export and three more documents (cargo dispatch document, commercial invoice, and packing list) are required to import. And, while it takes 11 days to comply with all the procedures required to export or import goods in Japan, it takes only 6 days to comply with the procedures required to export and 5 days to comply with the procedures required to import in Denmark, United States, and Estonia. The cost associated with procedures required to export (import) is 34% (42%) lower in Hong Kong than in Japan.

To improve its ranking on the ease of trading across borders, Japan can:

- *allow electronic submission and processing (reform 2.8.1)*
- *link agencies through an electronic single window (reform 2.8.2)*
- *use risk-based inspections (reform 2.8.3)*
- *improve transparency in trade regulation (reform 2.8.4)*

Allow electronic submission and processing: Electronic systems for filing, transferring, processing, and exchanging customs information have become an important tool for managing flows of information in complex trading systems. The newest web-based systems can allow Japanese exporters and importers to submit their documents from anywhere and to pay duties online. Japan can update its regulatory framework to allow exporters and importers to take advantage of the new information technologies. Over the past 9 years, 119 economies have introduced or improved such systems. Today traders can submit all trade documents electronically in more than half of OECD high-income economies with no need to provide hard copies. For example, France speeded up and simplified its customs clearance procedures by introducing an electronic customs declaration and eliminating the need to submit certain documents. The Netherlands made importing easier by introducing a new web-based system for cargo release at the port terminals in Rotterdam. Spain also expanded the use of electronic submission of customs declarations.

Link agencies through an electronic single window: Increasingly, economies are going a step further by virtually linking not only traders and customs but all agencies involved in trade and transport through an electronic single-window system. In what is considered the best practice today, such a system allows traders to file standard information and documents through a single entry point to fulfill all import, export and transit-related regulatory requirements, and shares relevant information with all parties involved including private participants such as banks and insurance companies as well as public agencies such as immigration and vehicle registration authorities.

As of this writing, 71 economies around the world have implemented single-window systems of varying complexity.¹⁷ In Singapore, the government established the world's first national single window for trade (TradeNet) in 1989, bringing together more than 35 border agencies.¹⁸ Portugal also implemented an electronic single window for port procedures. The Korea Customs Service estimates that the introduction of a single-window system there brought some \$18 million in benefits in 2010, a part of the overall economic benefits that year of up to \$3.47 billion from the agency's trade facilitation efforts.¹⁹ Indeed, for Korean-based companies such as Samsung and LG, achieving rapid and predictable turnaround times is an important source of their competitiveness.

Use risk-based inspections: Requiring imports and exports to undergo inspections (for tax, security, environmental, border control, and health and safety reasons) is often necessary. Done with a heavy hand, however, inspections can be a serious obstacle to efficient and predictable trades.

Over the years, customs administrations around the world have developed systems for establishing risk profiles of products that allow them to apply inspections in proportion to the potential risk. Investing in equipment is another way to help expedite the processing of cargo. Many economies have adopted the use of scanners to limit the need to physically open containers. In some countries, however, the use of scanners has led to further delays because customs agents scan all containers and mandatory scanning fees have added costs for traders. Efficient use of scanners in conjunction with risk-based profiling can strike the right balance in inspection, contributing to the efficiency of the trade process. Risk-based inspections are the norm in OECD high-income economies, but Japan has not adopted the practice. They are also becoming increasingly common elsewhere. Today 134 economies use risk-based inspections.

Improve transparency in trade regulation: Improving transparency in trade regulation by providing easy access to documentation of requirements and tariff schedules can reduce transactions costs for importers and exporters. The average customs clearance cost for exports as measured by Doing Business is 25.3% lower in those economies where documentation requirements are easily accessible.²⁰

2-9. Enforcing contracts

Japan currently ranks 19th out of 31 on this index. The Doing Business Enforcing Contracts indicator measures time, cost and procedural complexity to enforce a debt in court between two local businesses. It takes 360 days (or nearly 1 year) from the moment a case is filed until the creditor receives payment and the average cost amounts to 32.2% of the value of the claim.

Effective commercial dispute resolution has many benefits. Courts can be important for entrepreneurs because they interpret the rules of the market and protect economic rights. Efficient and transparent courts encourage new business relationships because businesses know they can rely on the courts if a new customer fails to pay. Speedy trials are essential for small

¹⁷ World Bank Doing Business 2014 Database

¹⁸ Singapore Customs Service. 2007. *Annual Report 2006/07*. Singapore. <http://www.customs.gov.sg/>

¹⁹ See Korea Customs Service (2011)

²⁰ World Bank Doing Business 2014 Database

enterprises, which may lack the resources to stay in business while awaiting the outcome of a long court dispute.

To improve its rankings on this indicator, Japan can:

- *limit adjournments and make enforcement of judgments more efficient (reform 2.9.1)*
- *introduce performance measures for judges (reform 2.9.2)*
- *maintain specialized commercial court, division or judge (reform 2.9.3)*
- *expand case management systems and automation (reform 2.9.4)*

Limit adjournments and make enforcement of judgments more efficient: Judges can limit adjournments. Frequent adjournments slow down contract enforcement in Japan. Adjournments are responsible for 280 days out of the 360 days that it takes to get trial and a judgment, and add another 60 days for enforcement. Time limits should be enforced to reduce long delays in court hearings.

Introduce performance measures for judges: Performance evaluation for judges could be introduced. There are several indicators for the judge performance used in other countries. One of them is the disposition rate, which is calculated by dividing the number of disposed cases (by issuing judgments or settling a case in mediation) by the number of incoming cases .

Maintain specialized commercial court, division or judge: Austria and Belgium have stand-alone commercial courts. The U.K. and the U.S. have specialized commercial divisions within their courts. Specialized courts have been found to improve efficiency.²¹ Creating specialized commercial courts can result in faster and less costly contract enforcements. One reason for the greater efficiency is that judges become expert in handling commercial disputes. Commercial courts often have less formal procedures. For example, use of oral arguments is permitted even where the general courts require written procedures.

Expand case management systems and automation: Japan could expand the use of case management that currently exists in minimal form and only in limited number of courts. Judicial case management involves monitoring and managing cases in the court docket from the filing of the claim until judgment is rendered. It has proved to be an effective tool for reducing procedural delays at court and for monitoring the performance of judges and court officers. By analyzing court workloads, case management systems can help predict trends and allocate resources strategically. Case management can be particularly successful when courts are computerized and when support functions (such as electronic filing, case tracking, document management, deadline reminders and scheduling of hearings) are all performed automatically. Currently 21 of the 189 economies covered by Doing Business allow electronic filing of the initial complaint in a commercial case. In 12 economies including Korea and Malaysia, the capacity has been introduced only after 2007.

2-10. Resolving insolvency

²¹ See Botero et al (2003).

The Doing Business resolving insolvency indicator identifies the main procedural and administrative bottlenecks in the bankruptcy process. Economies with good bankruptcy procedures can maximize the total value of recovered debt (to be divided among the debtor, the main creditors and possibly the shareholders) with the least cost. Economies with inefficient insolvency procedures have low recovery rates.²² An efficient bankruptcy procedure helps keep economically viable firms in business and encourages creation of new firms, thereby promoting healthy competition in the economy.

Japan already ranks first in the world on this indicator. To sustain its ranking on the ease of resolving insolvency, Japan can:

- *promote specialized courts (reform 2.10.1)*

Promote specialized courts: Promoting specialized courts is among the most efficient ways to ensure that insolvency cases receive attention more quickly. It also improves the quality of the judicial system, because it allows judges to specialize in hearing insolvency cases and thus better equips them to make informed decisions. Japan could reduce the length of proceedings to shorter than 0.6 years by creating courts specialized in bankruptcy cases.

3. What would it Take for Japan to be in Top Three?

Overall, we have identified 27 reforms that Japan can carry out to reduce the cost of doing business. In this section, we classify each reform according to two dimensions. One is whether the reform requires legal changes or not. The other is whether the reform would face strong political resistance. Thus, we group the reforms into four groups as in Figure 1. It seems safe to assume that the reforms in Group I are much easier to implement than those in Group IV. Whether the reforms in Group II (legal changes that do not face strong political resistance) are easier to implement than those in Group III (administrative changes that face strong political resistance) is debatable, but we assume it is the case.

Table 2 summarizes our judgment about how each reform is classified along the two dimensions. Of the 27 reforms, we find 15 reforms to be just administrative changes and not likely to face strong political resistance. For example, allowing electronic submission and processing of export and import documents would entail only an administrative change in the process. Similarly, elimination of the requirement for company seal and judicial scrivener to complete the registration procedure on behalf of the company can be done without changing any existing law. Moreover, these reforms are not likely to face much political resistance because the benefactors of the regulations (seal makers and judicial scriveners in this example) are not known for their political clout. Introducing fast-track procedures and combining certain procedures within the property transfer process at the Legal Affairs Bureau do not require legal changes and are not likely to face serious political resistance, either. Such reforms are classified into Group I.

²² See Crimizi et al (2012)

Certain administrative reforms may face political resistance. We find 2 of the 27 reforms fall into this category. Creating a one-stop shop for business registration requires a collaborative effort from more than one government agencies (the Ward Office, Ministry of Justice, District Tax Office, Municipality, Labor Standards Inspection Office, Japan Pension Service, and Public Employment Security Office). These agencies would lose some of their powers in the consolidation process and hence would oppose the reform. Similarly, forcing TEPCO to make internal reforms to improve the efficiency in the process of getting an access to electricity can be a challenge. These reforms that are administrative in nature but are likely to face substantial political resistance are classified into Group III.

There are 10 reforms that require legal changes. Two of those (reduction of the business registration fee and reduction of the property registration fee) would not face strong political resistance. On the contrary, these fee reducing reforms are actually likely to be very popular. These are classified into Group II.

The remaining 8 reforms that require legal changes would be politically difficult. For instance, enhancing required disclosure, making it easier to sue directors, and opening company books for shareholder inspection would all involve changing the Corporate Law. We can easily expect strong opposition from many corporations. Similarly, reducing number of tax payments by consolidating some taxes and social security contributions require legal changes, and will face strong oppositions from the social security agencies that would lose some powers. These reforms are classified into Group IV.

Table 3 summarizes how all the reforms are classified into four groups. In terms of the number, most of the reforms require only administrative changes and are not expected to face high political resistance. This is good news for the Japanese government. These reforms are relatively easy to implement.

Implementing just those reforms in Group I, however, is not sufficient to make Japan one of the top three countries in the ease of doing business ranking. Even if we assume all the other countries that are ranked higher than Japan currently do not do anything to improve their conditions for doing business, Group I reforms improve Japan's ranking to just #9. Japan would leapfrog Estonia, Germany, Canada, Ireland, Sweden, and Iceland, but would still be ranked lower than New Zealand, the U.S., Denmark, South Korea, Norway, United Kingdom, Australia, and Finland.

Implementing all the reforms that are not likely to face tough political resistance (Groups I and II) would still be insufficient. It would improve Japan's ranking to #4, not quite top three. Japan would be still looking up New Zealand, the U.S., and Denmark.

Only by implementing all the reforms except for those that require legal changes and are expected to face high political resistance, Japan would be able to make the top three. Even this may not be sufficient, however, if the other countries do not stand still. The assumption that other countries will not do any reforms will certainly turn out to be false. Thus, Japan needs to implement at least all the reforms in Groups I, II, and III, and most likely some in IV, if it wants to be among the top three countries in the ease of doing business ranking.

4. Concluding remarks

Improving the environment for business is an important part of the growth strategy (Third Arrow) of Abenomics. As the KPI (Key Performance Indicator) for this effort, the Abe Administration aims to improve Japan's rank in the World Bank Doing Business Ranking from the current #15 among high-income OECD countries to one of the top three.

Setting a clear target makes sense because the experience of business regulatory reforms elsewhere shows measuring and monitoring the progress of reform is important. For instance, Saudi Arabia used the doing business indicators as part of a scheme to measure its reform progress. In 2005, it set up a 5-year investment climate reform program and aimed to be among the top 25 in the doing business ranking by 2008.²³ The reform program was successful and Saudi Arabia was ranked 11th in the World Bank Doing Business 2011 report.

Although the goal may be clear, it is not yet clear how the Japanese government will try to improve its Ease of Doing Business ranking. This paper clarifies what it takes for Japan to be among top three countries in terms of ease of doing business. By looking at details of the World Bank Doing Business ranking, we identify various reforms that Japan could implement to improve the ranking. Then, we classify the reforms that we suggest into four groups depending on whether the reform requires legal changes and whether the reform is likely to face strong political resistance.

By just doing the reforms that do not require legal changes and are not likely to face strong political opposition, Japan can improve the ranking from the current 15th among high-income OECD countries to #9. To be in top 3 is more difficult. Japan would need to implement all the reforms that we suggest except for those that require changing the laws *and* are likely to face strong political resistance, even under the unrealistic assumption that the other countries do not reduce the cost of doing business. Thus, in order to achieve the KPI becoming one of the top three countries among high-income OECD countries in terms of ease of doing business, Japan would need to carry out all the reforms in Groups I, II, and III, and most likely some in Group IV as well.

Improving the business environment is just one of the many economic reform areas proposed in Abenomics. Achieving the KPI for this reform area alone would not be sufficient to restore the growth to Japan. It will be important to have clear KPIs for other growth enhancing reform areas and to achieve those. A current problem of Abenomics is that it is not clear on how to achieve the KPIs in many reform areas even when they have clear KPIs. This paper shows a way to formulate a clear reform plan to achieve the KPI for improving the business environment in Japan. Similar exercises would be very useful in other reform areas as well.

²³ See Belayachi and Haidar (2008)

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Table 1: Japan's performance and top 5 OECD economies in terms of ease of doing business

	Japan ranking in the		Ranking of the top 5 countries in OECD (from first to fifth)
	World	OECD	
Starting a Business	120	28	New Zealand, Canada, Australia, Ireland, Netherlands
Dealing with Construction Permits	91	21	Denmark, Australia, New Zealand, Germany, South Korea
Getting Electricity	26	10	Iceland, South Korea, Germany, Switzerland, Sweden
Registering Property	66	22	New Zealand, Denmark, Norway, Slovak Republic, Iceland
Getting Credit	28	9	United Kingdom, New Zealand, United States, Australia, Poland
Protecting Investors	16	8	New Zealand, Canada, United States, Ireland, United Kingdom
Paying Taxes	140	31	Ireland, Canada, Denmark, United Kingdom, Luxembourg
Trading Across Borders	23	14	South Korea, Sweden, Estonia, Denmark, Finland
Enforcing Contracts	36	19	Luxembourg, South Korea, Iceland, Norway, Germany
Resolving Insolvency	1	1	Japan, Norway, Finland, Netherlands, Belgium
Ease of Doing Business	27	15	New Zealand, United States, Denmark, South Korea, Norway

Note: The source of this information is the World Bank 2014 Doing Business Database.

Table 2: Expected impact and political resistance of recommended reforms

Reform name	Reform type	Impact	Expected political resistance
Starting a business			
<i>Eliminate the requirement for a company seal (reform 2.1.1)</i>	Administrative	. Cut 4 days, 2 procedures, and cost by 0.53% of income per capita. . Improve ranking by 2 points	Low
<i>Make business registration administrative (reform 2.1.2)</i>	Administrative	. Cut 7 days . Improve ranking by 2 points	Low
<i>Create one-stop shop for business registration (reform 2.1.3)</i>	Administrative	. Cut 7 procedures and 21 days . Improve ranking by 7 points	High
<i>Cut registration fees (reform 2.1.4)</i>	Legal	. Cut cost by 6.8 % of income per capita . Improve ranking by 2 points	Low
Dealing with construction permits			
<i>Reduce number of permits (reform 2.2.1)</i>	Administrative	. Cut 7 procedures . Improve ranking by 3 points	Low
<i>Introduce statutory time limits (reform 2.2.2)</i> <i>Limit inspections (reform 2.2.3)</i>	Administrative	. Cut 130 days . Improve ranking by 6 points	Low
Getting electricity			
<i>Improve process efficiency (reform 2.3.1)</i>	Administrative	. Cut 80 days . Improve ranking by 3 points	High
Registering property			
<i>Introduce fast-track procedures (reform 2.4.1)</i>	Administrative	. Cut 7 days . Improve ranking by 1 point	Low
<i>Combine and eliminate some procedures (reform 2.4.2)</i>	Administrative	. Cut 2 procedures (days will not change as those procedures are simultaneous) . Improve ranking by 3	Low
<i>Lower registration fees (reform 2.4.3)</i>	Legal	. Reduce cost to 0.2 % of property value . Improve ranking by 2 points	Low
Getting credit information			
<i>Extend security rights (reform 2.5.1)</i>	Legal	. Provide more credit information and stronger legal rights for borrowers and	High

		lenders . improve ranking by 1 point	
<i>Index the collateral registry by debtors' names (reform 2.5.2)</i>	Legal	. Provide more credit information for lenders . Improve ranking by 1 point	High
<i>Pay secured creditors first after liquidation (reform 2.5.3)</i>	Legal	. Provide stronger legal rights lenders . Improve ranking by 1 point	High
Protecting investors			
<i>Increase disclosure requirements (reform 2.6.1)</i>	Legal	. Protect minority shareholders more . Any (or all) of these 3 reforms in this (protecting investors) area will have same impact and improve ranking by 2 points	High
<i>Make it easier to sue directors (reform 2.6.2)</i>	Legal	. Same as above	High
<i>Open company books for shareholder inspection (reform 2.6.3)</i>	Legal	. Same as above	High
Paying taxes			
<i>Reduce number of payments (reform 2.7.1)</i>	Legal	. Reduce number of payments (to 4) and hours needed to pay taxes (to 150) . Improve ranking by 7 points	High
<i>Reduce corporate profit tax rates (reform 2.7.2)</i>	Legal	. Reduce profit tax rate to below 34% from its current 49.7% . Improve ranking by 3 points	High
Trading across borders			
<i>Allow electronic submission and processing (reform 2.8.1)</i> <i>Link agencies through an electronic single window (reform 2.8.2)</i> <i>Use risk-based inspections (reform 2.8.3)</i> <i>Improve transparency in trade regulation (reform 2.8.4)</i>	Administrative	. Reduce time, number of documents, and cost needed to import and export to 5 days, 2 documents, and 600 USD, respectively . Improve ranking by 3 points	Low
Enforcing contracts			
<i>Limit adjournments and enforce judgments (reform 2.9.1)</i>	Administrative	. Reduce time to 150 days . Improve ranking by 2 points	Low

<i>Introduce performance measures for judges (reform 2.9.2)</i> <i>Maintain specialized commercial court, division or judge (reform 2.9.3)</i> <i>Expand case management systems and automation (reform 2.9.4)</i>			
Resolving insolvency <i>Promote specialized courts (reform 2.10.1)</i>	Legal	Japan is already ranked first	High

Table 3: Classification of Reforms for Japan

		Political resistance	
		Low	High
Reform type	Administrative	2.1.1 2.1.2 2.2.1 2.2.2 2.2.3 2.4.1 2.4.2 2.8.1 2.8.2 2.8.3 2.8.4 2.9.1 2.9.2 2.9.3 2.9.4	2.1.3 2.3.1
	Legal	2.1.4 2.4.3	2.5.1 2.5.2 2.5.3 2.6.1 2.6.2 2.6.3 2.7.1 2.7.2

Figure 1. Classification of Reforms

		Political Resistance	
		Low	High
Legal Change	Not Necessary	Group I	Group III
	Necessary	Group II	Group IV