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Japanese Media Look at Tax-Free Savings Reform

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Summary

The Liberal Democratic Party (LDP) decision to include repeal of a major tax-exempt savings system in an overhaul of the tax system surprised Japanese journalists, who thought the program was too popular for the LDP to tackle. Political pundits in Tokyo view the LDP decision as a major victory for Nakasone, and attribute his success to a clever political deal involving a trade-off on the sensitive rice price issue. In addition, the Japanese media have highlighted the positive role the contenders to succeed Nakasone played in securing party approval for the move. Opposition parties and liberal journalists continue to denounce the proposed changes as "favoring the rich at the expense of the poor," but most Japanese commentators--along with a majority of business leaders--approve of the LDP action, and believe that it will accelerate the deregulation of interest rates. Nonetheless, the fate of the proposal to tax savings is currently being held hostage to the outcome of a battle over introduction of a controversial sales tax.

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The Nakasone Team Scores

LDP proposals unveiled in December will--if enacted--abolish the 60-year-old Maruyu system, under which each Japanese citizen can deposit up to \$19,000 in a tax-free savings account at any one of the nation's 18,000 post offices.¹ Although immensely popular with the public as well as postmasters--who earn a commission on deposits--economists from several countries have criticized tax-free savings accounts for lowering Japanese consumer spending. Moreover, most observers agree the system invites abuse. For example, one person in Tokyo reportedly has used pseudonyms to establish 21 accounts totaling \$370,000, and a doctor in Hiroshima has hidden his savings of \$1.4 million in 82 accounts in two prefectures. [REDACTED]

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When the LDP began a debate on the future of the Maruyu system in the summer of 1986, the Japanese media were skeptical that the ruling party would endorse sweeping reform of the popular system. Their skepticism stemmed in part from the party's reluctance to follow through on previous proposals--most recently in 1984--to make tax-free saving provisions less generous. In addition, in the fall of 1986, Japanese political analysts contended that the number of Maruyu supporters within the party was growing. For example, they pointed out that 400 LDP members attended a convention in November 1986 sponsored by opponents of reform. A prominent participant was Deputy Prime Minister Shin Kanemaru, the most influential of the postal savings lobbyists. [REDACTED]

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In hindsight, however, the media are painting the party members' campaign to protect the Maruyu system as a smokescreen. After reading transcripts of meetings of the LDP Tax Council, as well as meetings involving the entire party, Japanese journalists now believe that a deal involving reform of the Maruyu system was struck as early as last summer. More specifically, several press items suggest that the government's decision to maintain the current rice price paved the way for abolition of the Maruyu system. [REDACTED] farmers have been the primary beneficiaries of the current system, because in the small villages in which they live few savings alternatives exist. The repeal of Maruyu, therefore, will hurt this important LDP constituency. To lower the price of rice about the same time--as Nakasone had planned--would have been doubly damaging to farmers and to LDP members with strong farm support. The media consider the LDP's decision in August 1986 to maintain the current price of rice for another year to be a peace offering that allowed the LDP Tax Council to proceed with plans to abolish the Maruyu system. [REDACTED]

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¹ The tax-free status on the interest earnings of postal savings and some bank deposits will be continued for people aged 65 and older, fatherless families, socially disadvantaged, and the handicapped. [REDACTED]

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[redacted]

Bureaucratic equities in the Maruyu system also required the LDP to make deals among affected ministries before unveiling the proposal:

- The media note that the Finance Ministry, a long-time opponent of Maruyu, will be the biggest winner, standing to gain additional annual tax revenues of approximately \$85 billion.
- The biggest loser--the Ministry of Post and Telecommunications (MPT), which has nominal jurisdiction over the postal saving system's \$645 billion in assets--won an important concession. It will be allowed to invest some postal savings funds--nearly \$7 billion worth in the initial year--at its own discretion rather than to channel them through the fiscal investment and loan program, which provides funding for the Japan Development Bank, Housing Loan Corporation, and other official financial institutions.
- Postmasters also won the right to sell government bonds if the Maruyu changes are implemented. Postmasters would earn commissions on bond sales, and this would compensate for lost commissions as the appeal of postal savings accounts faded.² [redacted]

The New Leaders: Unsung Heroes?

Although the press is playing the Maruyu decision as a personal victory for Nakasone, it also is noting that the move demonstrated the political clout of Nakasone faction member Sadanori Yamanaka as well as of the "new leaders" who hope to succeed Nakasone--LDP Secretary General Takeshita, LDP Executive Council Chairman Abe, and Finance Minister Miyazawa. Yamanaka is widely known for the major role he played in the reform of the Anti-Monopoly Law in 1976. The Japanese press has regarded him as Nakasone's "hatchetman" in the area of taxes since he was appointed chairman of the LDP Tax Council last summer. Journalists attribute the new leaders' support for Maruyu reform to their desire to get the controversial measure out of the way before they come to power:

² Interest income from up to \$19,000 on principal in bank deposits, investment trusts, and government bonds has enjoyed the same tax-exempt status, but the institutions offering these investments possess an array of higher yielding investment vehicles and therefore are in a position to win investors away from postal savings if all tax exemptions are abolished. [redacted]

- Abe has been the most outspoken of the three on the need for reform. Along with Chief Cabinet Secretary Gotoda, he publicly criticized MPT officials for lobbying against repeal of the system in meetings with LDP members, labeling such tactics as meddling in party business. Abe also was instrumental in convincing one of the Tax Council members from his faction, Akira Fukida, to support the new policy.
- Takeshita initially followed a strategy of quietly containing antireform elements, but he dominated the final meeting on the issue and came out categorically against maintaining the Maruyu system.
- Miyazawa was given credit for actively collaborating with Nakasone and Yamanaka by garnering the support of his faction, which pleased not only the Prime Minister but also bureaucrats in the Finance Ministry. Political observers suggest that as a result of this cooperative effort, if Miyazawa becomes the next prime minister, he is likely to name Yamanaka his finance minister.

The Fallout From Reform

Editors foresee temporary confusion among financial institutions if the proposed reform bill is implemented. Japan's financial community also expects the end of Maruyu to spark major shifts in funds among institutions. Not surprisingly, financiers who believe their institutions will benefit from these shifts have come out in favor of the LDP decision:

- Securities firms generally welcome the reform as a possible new stimulus to the stock market.
- In general, private-sector banking institutions are united in support of abolishing postal savings' tax-free status, calculating that the change would make bank rates for deposits look more competitive.

Most commentators believe Maruyu reform will accelerate the deregulation of Japanese domestic interest rates. But they doubt that abolishing Maruyu will boost consumption--and thus imports--enough to quickly reduce Japan's massive trade surplus.

Despite the generally upbeat assessments of the Maruyu reform, the media believe the proposal's fate is being held hostage to controversy over other provisions of the tax reform bill. More specifically, a major element of the package, introduction of a 5-percent sales tax, has generated widespread dissension. The opposition parties have so far maintained a unified front to block passage of any tax legislation in the Diet. Although Nakasone's reform package has been denounced even by his long-time friend, the president of the Japan Chamber of Commerce, as well as some of his own party members, prominent observers in Tokyo believe Nakasone will get his tax reform by the summer at the earliest. Some analysts, however, caution that it is at least conceivable

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that Nakasone may be forced out of office before the summer in exchange for passage of the reform bill. [Redacted]

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SUBJECT: Japanese Media Look at Tax-Free Savings Reform [Redacted]

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