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On general subjects the Bureau brings out publications of documentary character in the Series: "Publications of the International Bureau of Fiscal Documentation," and in the Series "Studies on Taxation and Economic Development."
These series have been supplemented by various special publications. Since 1961 the Bureau has published *European Taxation*, at first as a fortnightlyEnglish language review of tax developments on the European Continent, in the United Kingdom and in Ireland, but since January, 1965 as an expanded monthly periodical. A new loose-leaf, "Tax News Service", first published in 1965, brings rapid information of world-wide tax developments. Two loose-leaf services were started in 1963: "Supplementary Service to European Taxation" and "Guides to European Taxation". The latter series includes three published volumes:
"The Taxation of Patent Royalties, Dividends and Interest in Europe", "Corporate Taxation in the Common Market" and "The Taxation of Private Investment Income".
In 1966, a new loose-leaf service was started: "Tax Treaty Guides". The first volume is "Handbook on the United States-German Tax Convention".

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«Régime fiscal des redevances, dividendes et intérêts en Europe», «L'imposition des sociétés de capitaux dans les pays du Marché Commun» et «L'imposition de revenu des investissements privés».
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INTRODUCTION

From the beginning of the XXIst. Volume, the Bulletin is being published in a new form with the contents suitably adapted to its new appearance. As in 1966 the Bulletin will continue the policy of containing more articles and documentation underlining the reasons behind tax revisions and directives, etc., with particular emphasis on developments in the sphere of international tax law. Supplements to the Bulletin, giving informative documentation, will appear every two months together with the Bulletin of that month.

This issue contains a Supplement on the project of the multilateral convention between the French speaking Africain countries.

Since "Tax News Service", a fortnightly publication of the International Bureau of Fiscal Documentation, took over the publication of brief articles on tax news, these kinds of articles will no longer be published in the Bulletin.

Regularly included in the Bulletin are:
Articles, Documents, Developments in international tax law, Bibliography—with cumulative index.

The languages of the Bulletin remain English, French and German.

INTRODUCTION

Au début de la 21e année de sa parution le Bulletin revêt une nouvelle forme aussi bien dans sa présentation que dans son contenu. Poursuivant le chemin déjà suivi en 1966, le Bulletin contiendra plus d'articles, plus de documentation sur les raisons des réformes et des directives fiscales. Une orientation permanente sera portée au domaine du développement fiscal international et en particulier aux pays sous-développés.

Sous forme d'information documentaire paraîtra tous les deux mois un Supplément au Bulletin. Ce sera, actuellement, le Supplément consacré à la convention fiscale multilatérale conclue entre les pays africains francophones.

L'information fiscale sous forme de courtes annonces ne figurera plus dans le Bulletin, mais deviendra exclusivement reservée à «Tax News Service».

Le Bulletin contiendra régulièrement les rubriques suivantes:
Articles, Documents, Développements de la législation fiscale internationale, Bibliographie — avec index cumulatif.

Les langues du Bulletin restent l'Anglais, le Français et l'Allemand.

GELEITWORT

Beim Anfang des XXIen Jahrganges erscheint das Bulletin in einem neuen Gewand. Auch der Inhalt ist der Erneuerung angepasst worden. Das Bulletin wird, den bereits im Jahre 1966 eingeschlagenen Weg folgend, mehr Artikel enthalten, ebenso wie Dokumentation welche die Begründung wichtiger Steuerreforme, Richtlinien u.s.w. angibt; der Entwicklung auf dem Gebiete des internationales Steuerrechts und des Steuerrechts der Entwicklungsländern wird stets Aufmerksamheit gewidmet.

Jede zwei Monate wird dem Bulletin ein Supplement hinzugefügt, das Dokumentarinformation gibt. Die heutige Nummer enthält ein Supplement über den Entwurf eines multilateralen Steuervertrages zwischen den französisch sprechenden afrikanischen Staaten.

Steuernachrichten im Sinne kurzer Aufsätze wird das Bulletin nicht mehr enthalten.

Diese Funktion ist vollständig von dem Organ „Tax News Service" übernommen worden, das zweimal per Monat veröffentlicht worden ist.

Das Bulletin ist in den folgenden Abteilungen eingeteilt:
Artikel, Dokumente, Entwicklungen im internationalen Steuerrecht, Bibliographie — mit Gesamtverzeichnis.

Die Verständigungssprachen bleiben englisch, französisch und deutsch.

* * * * ARTICLES * * * *

L. S. ULLMAN*:

ESTATE AND GIFT TAX PROVISIONS OF THE FOREIGN INVESTORS TAX ACT OF 1966[1]

After having first accumulated and then lost considerable "excess baggage"[2]) the Foreign Investors Tax Act of 1966 has finally emerged from the Congressional shuttle, a bit bruised, but still fairly attractive. This article will be limited to the estate and gift tax provisions of the new law. A discussion of the income tax provisions[3]) will appear in the work of Messrs. Roberts and Warren[4]). Accordingly, those provisions will not be considered here.

1. *Prior Law*

(a) *Estate taxes.* The United States has long imposed taxes on the estates of nonresident alien decedents in respect of property situated in the United States at the time of death at rates so high as to discourage investment in the United Stated by nonresident alien individuals. United States estate taxes were imposed on such U.S.-situs property at progressive rates scaled to a maximum of 77%.[5]) These rates were among the highest estate tax rates in the world.[6])

Moreover, the effective rates of U.S. tax in the case of that part of the estates of nonresident aliens situated in the U.S. were substantially higher than in the case of estates of citizens or residents.[7]) This discrepancy in tax burden resulted from several factors (1) denial of the marital deduction (whereby property passing to the spouse is not taxed if it does not exceed the value of 50% of the gross estate) in the case of the estates of nonresident aliens[8]), (2) a specific exemption of only $2,000 allowed to the estates of

*) Member of the New York Bar. Grateful acknowledgment is made to Donald R. Osborn and Willard B. Taylor of the New York Bar for reviewing the manuscript.

1) P.L. 89-809, Sections 108 and 109.

2) See the editorial, "Grandstanding on Taxes", The New York Times, October 6, 1966 at p. 46.

3) P.L. 89-809, Sections 101-107.

4) Roberts, Sidney I. and Warren, Willam C., "United States Income Taxation of Nonresident Aliens and Foreign Corporations" published by the Practicing Law Institute and the International Bureau of Fiscal Documentation (loose-leaf).

5) See Table I, *infra*.

6) See for comparative purposes the series relating to death and gift taxes in Europe which appeared in Volume 2 (1963) of *European Taxation* at p. 207 (France); in Volume 3 (1963) at pp. 3 (Spain), 15 (U.K.), 31 (Austria), 38 (Belgium), 82 (Netherlands), 99 (Portugal) and 103 (Sweden); in Volume 4 (1964) at pp. 3 (Italy), 44 (Germany) and 86 (Switzerland); and in Volume 6 (1966) at p. 159 (Norway).

7) See Table I, *infra*.

8) This further resulted in considerable discrimination as between the various foreign countries insofar as an exclusion of up to 1/2 the estate was allowed in respect of the estate of decedents who were residents of countries with community property laws, as in the case of most Spanish and Portuguese speaking countries.

nonresident aliens, as opposed to a $60,000 exemption in the case of U.S. citizens, and (3) denial of a tax credit to nonresident aliens in respect of foreign death taxes paid.

While the effective rates of U.S. estate taxes on property situated in the U.S. were higher than in the case of property of citizens or residents, the basis of the tax was not the same. Thus, deposits with U.S. persons carrying on the banking business and debt obligations issued by the United States, any State or subdivision thereof or by a U.S. corporation if such debt obligations were not physically situated within the U.S. at the time of death, were not included in the estate of nonresident alien decedents, although they were included in the estates of decedents who at the time of death were residents or citizens of the U.S.

One provision, unlike the above, was particularly favorable to nonresident aliens. It was the rule that full credits against Federal estate taxes were allowed for, among other things, State taxes paid even if the taxable estate for State estate tax purposes was substantially less than the taxable estate for Federal estate tax purposes (States generally do not impose estate tax on intangibles of nonresident decedents), and even if the rates of State estate taxes were considerably greater than the Federal rates.

The aforementioned inequities relating to the taxation of the estates of nonresident aliens vis-a-vis residents or citizens of the U.S. except as to the credit for foreign estate taxes paid, will be largely eliminated as the result of the recent enactment of the Foreign Investors Tax Act. The new Act will also effectively prevent citizens from expatriating for the purpose of availing themselves of the new reduced rates as nonresident aliens. Those results, however, differ considerably from the original purposes *(infra)* behind the efforts to amend U.S. taxation of the estates of nonresident aliens.

It is suggested that the inequities cited are not as severe as they may seem because the U.S. applies its progressive rates only to that part of the estate situated in the U.S. rather than computing the rate that would be applicable to the entire estate and applying that rate to that part of the estate situated in the U.S.

(b) *Gift taxes.* U.S. gift taxes are imposed generally on a cumulative basis at progressive rates scaled from 2 1/4% on aggregate taxable gifts of not over $5,000 to 57 3/4% on that part of the gift which exceeds $10,000,000. An exclusion is provided for the first $3,000 transferred by a donor (whether or not a resident or citizen) by gift to any person. In the case of residents or citizens of the U.S., a gift made by one spouse to any third party may be considered as made one-half by each spouse, provided that both spouses signify their consent in their gift tax returns. This "split gift" rule largely has the effect of doubling the exclusions and exemptions. A lifetime exemption for $30,000 is allowed only to residents or citizens.

Prior to the application of the new Act, nonresident aliens engaged in trade or business in the U.S. who transferred by gift intangible property situated in the U.S. were subject to U.S. gift tax. This was a tax which was in fact rarely levied because foreigners were generally unaware of its application and the Government was generally not apprised of taxable transfers when made. The new Act restricts the applicability of U.S. gift taxes with respect to intangibles owned by nonresident aliens.

2. *The Fowler Task Force Report.*

In accordance with his Balance of Payments Message of July 18, 1963[9]), President Kennedy on October 2, 1963 appointed a Task Force on "Promoting Foreign Investment in United States Corporate Securites and Increased Foreign Financing for United States Corporations Operating Abroad" headed by the then Under-Secretary of the Treasury, Henry H. Fowler (hence the name "Fowler Task Force"). On April 27, 1964 the Task Force submitted its report containing 39 recommendations to the President.[10])

Recommendation 29 of the Report was as follows:

"Eliminate U.S. estate taxes on all intangible personal property of nonresident alien decedents."[11])

The Recommendation was based on the belief that U.S. estate taxes were "one of the most important deterrents in our tax laws to foreign investment in the United States".[12]) This was hardly surprising in view of the limitations as to exemptions, credits and deductions in the case of estates of nonresident aliens under the then-existing provisions of the Internal Revenue Code.

It was also found that nonresident aliens could easily and legally avoid U.S. estate taxes by establishing a foreign holding company since the U.S. generally does not impose estate taxes on nonresident alien decedents in respect of stock held in foreign corporations whose assets consist in part of property situated in the U.S.[13]), whereas such property if owned directly by the nonresident alien decedent would be subject to U.S. estate taxes. It was indicated that the imposition of U.S. estate taxes on property situated in the U.S. when owned directly by a nonresident alien decedent but not when owned by certain foreign corporations the stock of which is owned at the time of death by a nonresident alien decedent was unrealistic.

The Recommendation of the Fowler Task Force was not followed, however, in legislation subsequently introduced in Congress. The creation of a foreign personal holding company therefore remains as a means of avoiding U.S. estate taxes.

3. *The Legislative History.*

After reviewing the Fowler Task Force report, the Treasury on March 8, 1965 submitted to the Congress a Bill (H.R. 5916) which, among other things, would have increased the $2,000 exemption for estates of foreign decedents to $30,000 and which would have substituted for the regular U.S. estate tax, rates of 5% on taxable estates of

9) See "Public Papers of the Presidents of the United States: John F. Kennedy—1963", published by the U.S. Govt. Printing Office, Wash., D.C. (1964) at p. 574.

10) Report to the President of the United States from the Task Force on "Promoting Increased Foreign Investment in United States Corporate Securities and Increased Foreign Financing for United States Corporations Operating Abroad." U.S. Govt. Printing Office: 1964.

11) *Id.* at p. 24.

12) *Id* at p. 25.

13) *Id.* at p. 24.

not over $100,000, $5,000 plus 10% on taxable estates of more than $100,000 but less than $750,000, and $70,000 plus 15% of any excess over $750,000.[14])

With certain exceptions, it would also have included for the first time in the basis for estate tax as property within the U.S. of nonresident alien decedents bonds not physically located within the U.S. at the time of death issued by domestic corporations or governmental units, but would have excluded foreign currency deposits in foreign branches of a domestic corporation.[15])

Special new provisions would have been provided that would expose to U.S. estate taxes the estate of nonresident aliens who within 10 years of their death lost their U.S. citizenship with, as one of the principal purposes of such loss, the avoidance of U.S. income, estate or gift taxes.[16])

It was stated in the Explanation to H.R. 5916[17]) that the proposed reductions would render the effective U.S. rates higher than those of France, Germany, The Netherlands and Switzerland, but substantially below those of the United Kingdom, Canada and Italy.[18])

As to the new bond situs rule, the Treasury Department Release[19]) indicated that the treatment of bonds should be the same as that of other debt obligations and that physical location of bonds is not a suitable way to determine their liability to an estate tax.[20])

After public hearings on the proposed Bill by the House Ways and Means Committee a new Bill (H.R. 11297) was introduced on September 28, 1965 by Congressman Mills, the Committee Chairman. Although no public hearings were held on H.R. 11297, many recommendations and comments were submitted to the Committee with respect to that Bill by interested parties. As a result of those submissions Congressman Mills introduced a further revised version of the proposed Foreign Investors Tax Act (H.R. 13103) on February 28, 1966. After public hearings, the Bill was reported out of the House Ways and Means Committee on March 7, 1966 and passed by the House without opposition on June 15, 1966.

The estate tax provisions of H.R. 13103 as passed by the House differed from the first Bill (H.R. 5916) in that the rates of estate taxes were increased from the 5-10-15 per cent rate schedule in the earlier bill *(supra)* to the following schedule of rates:[21])

14) H.R. 5916, Sections 8(a) and 8 (e).
15) H.R. 5916 Sections 8 (c) and 8 (d).
16) H.R. 5916 Section 8 (f).
17) See Vol. XIX, *Bulletin for International Fiscal Documentation*, p. 210 (1965).
18) That comparison of rates did not take into consideration the bases of the tax in the countries mentioned. Thus, for example, Germany and The Netherlands in addition to having lower rates apparently do not impose death duties on securities of domestic corporations held at death by nonresident aliens.
19) March 8, 1965: 7 CCH 1965 Stand. Fed. Tax Rep., Par. 6154.
20) Note, however, that in the event bonds of foreign corporations are physically situated in the U.S. at the time of death, the U.S. would still impose estate taxes on the value thereof. The argument cited is therefore a bit onesided.
21) H.R. 13103 (Union Calendar No. 631) Section 8(a).

TABLE I

If the taxable estate is	the tax is
Not over $100,000	5%
Over $100,000 but not over $500,000	$5,000, plus 10% of excess over $100,000
Over $500,000 but not over $1,000,000	$45,000, plus 15% of excess over $500,000
Over $1,000,000 but not over $2,000,000	$120,000, plus 20% of excess over $1,000,000
Over $2,000,000	$320,000, plus 25% over $2,000,000

The revised rates, according to the Report published by the House Ways and Means Committee[22]) and later echoed in the Report of the Senate Finance Committee[23]), were designed to result in approximately the same treatment of estates of nonresident aliens as in the case of decedents who at their death were United States citizens entitled to the maximum marital deduction. It was estimated that the new reduced rates would result in a revenue loss to the U.S. of approximately $3,000,000.[24])

The comparison of effective rates of United States estate taxes on the estates of nonresident alien decedents with property in the U.S. and on the estate of decedents who were U.S. citizens under prior law and under the new Act is illustrated in the following table[25]):

TABLE II

Effective Rate of Tax

	Nonresident alien		*U.S. Citizen*	
U.S. gross estate [26])	Prior treatment	Tax treatment provided by the new Act [27])	With marital deduction	Without marital deduction
$ 2,000				
$ 10,000	2.9			
$ 30,000	7.7			
$ 60,000	12.5	2.0		
$ 100,000	17.3	3.0		3.0
$ 500,000	25.8	7.4	8.0	22.1
$ 1,000,000	28.8	10.1	11.1	26.7
$ 5,000,000	43.0	17.8	16.9	42.3
$10,000,000	53.3	20.6	21.2	52.8

22) H.R. No. 1450, 89th Cong. 2d Session at p. 42.
23) Senate Report No. 1707, 89th Cong. 2d Session at p. 50.
24) *Id.* at p. 10.
25) *Id.* at p. 43.
26) For purposes of these computations it is assumed 10% of gross estate is deducted for funeral and other expenses, both in the case of U.S. citizens and nonresident aliens.
27) Takes into account the increase in the exemption from $2,000 to $30,000.

The new Bill also included provisions concerning the imposition of U.S. estate taxes on deposits with persons carrying on a banking business in the U.S. owned at the time of death by nonresident alien decedents. Such deposits had been considered under the then-existing law as having a situs outside the U.S. for estate tax purpose.

After passage by the House, H.R. 13013 was sent to the Senate. When reported out of the Senate Finance Committee on October 4, the Bill had been revised in important details from the House-passed version. In addition the Bill now carried a host of special interest measures which were added to the Bill as amendments. The amendments, numbering 25 or so, were designed, among other things, to aid the aged with their drug bills, Presidential candidates with their campaign expenses and clam diggers with their depletion allowances.[28])

The Bill was approved in the Senate by a vote of 58 to 18 on October 13, 1966, after some floor skirmishes concerning some of the unrelated amendments.[29])

In the estate tax area the only major change adopted by the Senate was a delay in the application of U.S. estate taxes to deposits with persons carrying on a banking business in the U.S. from the effective date of the Act as under the House passed Bill, to the estates of nonresident aliens whose death occurs after December 31, 1971. It was stated in the Senate Finance Committee Report[30]) that the House Bill was amended to conform this estate tax provision to the effective date of the income tax provision which taxes the interest from such deposits after December 31, 1971.[31]) That amendment could also be viewed as a concession to considerable criticism from banks, investment banks and others directly interested in the matter.[32]) At any rate the provision is clearly opposed to the original Fowler Task Force proposal and to the balance of payments anxieties which gave rise to that Task Force and later to the first Bill.

The Senate and House versions of the Foreign Investors Tax Act were sent to a Conference Committee composed of members of the Senate and members of the House. The measure was reported out of the Conference Committee on October 19, 1966 with only 12 riders of the original 25, and with one amendment in the estate tax area. The effective date in respect of the taxability for estate tax purposes of deposits with persons carrying on a banking business in the U.S. was delayed one year so as to apply to estates of persons dying after December 31, 1972.[33]) It was expressly stated in the Conference Re-

28) See H.R. 13103 (Calendar No. 1675) Title II—"Other Amendments to Internal Revenue Code", Title III—"Presidential Election Campaign Fund Act", and Title IV—"Miscellaneous Provisions".

29) "The Wall Street Journal", Oct. 13, 1966, p. 32 column 1.

30) Op. cit. supra footnote 23 at 52.

31) H.R. 13103 (Calendar No. 1675) Section 102 (a) (1).

32) See, for example, the statement to the Senate Finance Committee by the Foreign Investment Committee of the Investment Bankers Association of America, dated Aug. 8, 1966 (mimeograph).

33) Conference Report, H.R. No. 2327 89th Cong., 2d Sess. at pp. 6 and 7. Note that the income tax provisions relating to the taxation of interest on deposits were also changed so as to apply after December 31, 1972.

port[34]) that the insertion of December 31, 1972 as the termination of the (income tax) exemption for interest on bank deposits would provide an opportunity to review the exemption in view of developments in the balance-of-payments situation and other factors. It is presumed that the comparable exemption from estate tax of deposits with persons carrying on a banking business in the U.S. deposits might also be reviewed in the light of those factors.

The House agreed to the Conference Bill on October 20, 1966. On October 23, 1966 the Senate, after running into unexpectedly stiff opposition, passed the Foreign Investors Tax Act by a 31-22 vote. The unexpected opposition primarily concerned the campaign contribution provisions.

The President signed the Bill into law as P.L. 89-809 on November 13, 1966. In so doing, the President apparently ignored a plea of nine prominent professors of Federal tax laws who sent a telegram to the White House on October 29, 1966 urging that he veto the measure on account of the "extraneous last-minute riders" which "provide special benefits to limited groups."[35]) In signing the Act the President expressed deep regret that certain riders had been "engrafted on this vital legislation."[36]) He described the measure at his news conference held on November 13 as the "first major revision of the foreign investors tax structure in more than 30 years" and stated that the law would end "confusion and complexity", make tax treatment of the foreign investor "fairer and simpler" and remove tax "roadblocks which have discouraged foreign investments in this country."[37])

The gift tax provisions of the Foreign Investors Tax Act[38]) came out of the legislative mill in substantially the same form as when first introduced on March 6, 1965 in Section 9 of H.R. 5916. They were designed to exempt from U.S. gift taxes all transfers of intangible property by nonresident aliens. Under prior law such transfers were taxed if made by persons engaged in trade or business in the United States. The exemption would not apply to citizens who within 10 years of making such gift became expatriates with as a principal purpose thereof the avoidance of income, estate or gift taxes.

A special situs rule was provided in the case of debt obligations of U.S. corporations and of the United States, any State or subdivision thereof or the District of Columbia whereby such debt obligations would be considered as situated in the U.S., thus preventing an expatriate from benefitting from the rule otherwise applicable to the effect that nonresident aliens not engaged in trade or business in the U.S. are not subject to U.S. gift tax on intangible property.[39])

34) Conference Report op. cit. at pp. 6 and 7.
35) "The New York Times", October 30, 1966 p. 58 column 5. See also the editorial "Veto the 'Christmas Tree", "The New York Times", November 2, 1966, p. 44, column 1.
36) "The New York Times", November 14, 1966, page 1, column 8.
37) Ibid.
38) P.L. 89-809, Section 109.
39) Internal Revenue Code, Section 2501(a).

4. *Explanation of the Estate Tax Provisions of the Foreign Investors Tax Act of 1966.*

(a) *Rates of estate taxes.* Section 108 (a) of the new law replaces subsection (a) of Section 2101 of the Internal Revenue Code of 1954 ("the Code") with a new subsection (a). It amends the rates of estate taxes applicable to nonresident aliens in accordance with the schedule set forth in Table I *(supra)*.

(b) *Credits against U.S. estate taxes.* Section 108(b) amends Section 2102 of the Code by adding a new subsection (b) which provides a special limitation on the amount which may be credited against Federal estate taxes for State death taxes. The limitation provides a maximum credit for State taxes of an amount which bears the same ratio to the maximum credit allowable as the value of the property upon which a State death tax was in fact paid (and which is included in the gross estate for Federal tax purposes) bears to the value of the gross estate for Federal tax purposes. Thus, for example, if the taxable estate for Federal estate tax purposes is $250,000 consisting of real estate valued at $100,000 and taxed by State X at 5% and intangibles not taxed by any State valued at $150,000, the credit allowed for Federal estate tax purposes is that part of $5,000 (5% × $100,000) which $100,000 bears to $250,000, or $2,000.

(c) *Situs of debt obligations (including bank deposits).*

Under Section 108(c) of the new Act, Section 2104 of the Code is amended by adding a new subsection (c) which provides that debt obligations owned by nonresident alien decedents are includible in the gross estate if the primary obligor with respect to such debt obligation is the United States, any State or subdivision thereof, the District of Columbia or any U.S. person (a citizen or resident of the U.S., a domestic partnership, trust or estate, or a domestic corporation). This rule will only apply to estates of decedents dying after December 31, 1972 in the case of bank deposits with U.S. persons carrying on a banking business in the U.S., or with domestic branches of foreign corporations, if such branches are engaged in a commercial banking business.

By cross reference to new Code Section 861 (a) (1) (A), it is provided in Section 108(d) of the new Act that deposits or withdrawable accounts with banks, mutual savings banks, savings and loan and similar associations, and amounts on deposit with insurance companies will not be included in the estates of persons dying prior to January 1, 1973. Under prior law the I.R.S. had applied the exemption from U.S. taxes only to certain deposits with banks and certain savings and loan associations.

Under Section 108(d) deposits in foreign branches of domestic corporations or partnerships if such branch is engaged in a commercial banking business, will be considered as situated outside the U.S.

Debt obligations of a domestic corporation are not to be included if the interest on such obligations, whether or not actually paid, would be treated as income from sources without the U.S. under Section 861(a) (1) (B) of the Code (by reason of the fact that a specified percentage of the income of such corporation is from sources outside the United States). That exception is designed in part to cover indebtedness issued by subsidiaries formed primarily for the purpose of financing foreign operations, including

convertible debentures issued by such subsidiaries so long as the debentures are not converted into stock.

(d) *Exemptions.* Section 108(e) of the Act amends Section 2106 of the Code to increase from $2,000 to $30,000 the exemption allowed in the case of nonresident alien decedents.

If greater exemptions are provided by treaty, the treaty benefits shall apply.

(e) *Expatriation to avoid tax.* Section 108(f), relating to "Special Methods of Computing Tax," adds new Sections 2107 and 2108 to the Code. Section 2107(a) provides that persons who lost their citizenship after March 8, 1965 and within 10 years of the date of death will be subject to U.S. estate taxes at the same rates as those applicable in the case of citizens or residents unless such loss did not have as one of its principal purposes the avoidance of U.S. income estate or gift taxes.

The taxable estate is determined under Section 2107(b) in the manner applicable to nonresident alien decedents (i.e. property situated within the U.S.) with the exception that the fair market value of stock of a foreign corporation of which the decedent at the time of death owns directly or indirectly 10% or more of the voting power of all classes of stock entitled to vote and of which the decedent directly or indirectly owns or is considered (by attribution) to own more than 50% of the voting power of all classes of stock entitled to vote, is included in his estate in the proportion that the fair market value at the time of death of any assets owned by such foreign corporation and situated in the U.S. bears to the total fair market value of all assets owned by such corporation at that time.

Thus, for example, if a nonresident decedent who became an expatriate for the purpose of avoiding U.S. estate taxes owned at the time of death 30% of the voting stock in a foreign corporation with a fair market value of $100,000 and his wife also owned at the time of his death 30% of such stock (the wife's interest will be considered as owned by the husband for purposes of the application of this Section) and if 50% of the assets of such corporation were situated within the U.S., then $50,000 (50% × $100,000) is included in the gross estate for Federal estate tax purposes. If in the above example, the wife of the decedent owned only 15% of the voting stock of the foreign corporation at the time of the decedent's death, no U.S. estate taxes would be due since the stock owned and considered owned by the decedent would be less than 50% of the voting power. Similarly, he would not have been taxed if he owned 9.9% of the voting stock in such foreign corporation even if his wife owned the other 90.1%.

Credits will be allowed under subsection (c) for gift tax, tax on prior transfers and State estate taxes in the case of imposition of U.S. estate taxes on the estates of expatriates under the above rules. The credit for State estate taxes will be governed by the rules described in part 4(b) *supra*. It is provided in subsection (d) that Section 2107(a) will not apply in the case of loss of citizenship under certain sections of the Immigration and Nationality Act.[40])

40) 8 U.S. C. 1401 (b), 1482 and 1487 relating generally to failure to come to the U.S. prior to age 23 and to remain there for a continuous period of five years thereafter in the case of children born outside the U.S. to parents, one of whom is an alien; residence for a three year period by a person who

The burden of proof is placed in subsection (e) of Section 2107 on the executor of the estate of a person who has lost his citizenship after March 8, 1965 and within 10 years of the date of death if the Secretary first establishes that it is "reasonable to believe" that absent the above-described provisions such loss would result in a substantial reduction in taxes upon the transfer of such person's estate. The House Report[41]) indicates that a "tentative determination" based on the fact that a foreign country ordinarily imposes death taxes at substantially lower rates than would be imposed by the U.S. is sufficient to establish the reasonable belief.

(f) *Imposition of pre-1967 estate taxes.* New Section 2108 also added to the Code under the same Section 108(f) of the Act allows the President of the U.S. to proclaim that the benefits of the amendments contained in the new Act shall not apply to the estates of residents of a foreign country if he finds that (1) such country imposes more burdensome taxes on U.S. citizens who were not residents of such foreign country than are imposed under the new U.S. law on residents of such country, (2) such country fails upon request by the U.S. to revise or reduce such tax so that it is no more burdensome than the U.S. estate taxes, and (3) it is in the "public interest" to reimpose the pre-1967 estate tax provisions. The President is required under subsection (b) of Section 2108 to proclaim that the new reduced rates will apply in the event a foreign country against which a proclamation as described above has been previously issued no longer imposes more burdensome taxes.

In any event subsection (c) specifies that no proclamation may be issued unless the President notifies Congress of his intent to issue a proclamation 30 days prior to such proclamation.

It is indicated in both the House Report[42]) and the Senate Report[43]) that this section is in effect intended to provide the Government with an effective club in the negotiation of treaties.

(g) *Estate tax returns.* To reflect the increase of the exemption from $2,000 to $30,000 (see part 4d, *supra*) Section 6018(a)(2) of the Code provides that executors of nonresident alien decedents will only be required to file estate tax returns if that part of the gross estate which is situated in the U.S. exceeds $30,000.

(h) *Effective date.* Except as otherwise indicated (i.e. part 4c *supra* relating to the provisions concerning deposits in a U.S. bank (but not a foreign branch thereof) or in a branch of a foreign corporation if such branch is engaged in a commercial banking business in the U.S.)

acquired the nationality of the U.S. and a foreign country at birth in a foreign country of which he is a national by birth; and residence in a foreign country with or under the legal custody of a parent who loses his U.S. nationality under certain circumstances where no U.S. residence is established prior to age 25.

41) Op. cit. supra footnote 22 at p. 118.

42) *Id.* at p. 48.

43) Op. cit. supra footnote 23 at p. 56.

The estate tax provisions of the new Act shall apply to the estates of persons dying after the date of enactment.

5. *Explanation of the Gift Tax Provisions of the Foreign Investors Tax Act of 1966*

The gift tax provisions of the Foreign Investors Tax Act are included in Section 109 of the Act.

(a) *Transfer of intangibles.* Subsection (a) amends Section 2501(a) of the Code to provide an exemption from U.S. gift tax on the transfer by gift of intangible property (even if situated in the United States) by nonresident aliens (whether or not engaged in trade or business in the U.S.). The exemption will not apply, however, under the terms of Section 2501(a)(3) in the case of a donor who at any time after March 8, 1965 and within 10 years prior to the date of transfer lost his U.S. citizenship unless (1) such loss resulted from the application of certain sections of the Immigration and Nationality Act[44]) of (2) such loss did not have as one of its principal purposes the avoidance of U.S. income, estate or gift taxes.

Paragraph 4 of subsection 2501(a) provides a burden of proof requirement similar to that applicable with respect to expatriates under the estate tax provisions, discussed at part 4(e) *supra*. Here, too, a "tentative determination" that a foreign country would have imposed substantially lower taxes on such transfers than the U.S. would be sufficient to meet the government's threshhold requirement as to a reasonable belief that a principal purpose of such loss was tax avoidance, and this in effect shifts the burden of proof to the donor.

(b) *Situs of intangibles.* As in the case of estate taxes, the situs of debt instruments was heretofore considered for gift tax purposes to be at the place where the instrument was physically located. In order further to implement the pursuit of expatriates, it is now provided under Section 109(b) of the Act and Section 2511(b) of the Code that debt obligations of the United States, a State or any political subdivision thereof, the District of Columbia, or any United States person (a citizen or resident of the U.S., a domestic partnership, trust or estate or a domestic corporation) as well as shares of stock in a domestic corporation, owned by such persons will be deemed to be property situated in the U.S. and therefore subject to tax.

(c) *Effective date.* The amendments to the gift tax provisions of the Code shall apply to the calendar year 1967 and thereafter.

6. *Final Remarks*

The estate and gift tax provisions of the Foreign Investors Tax Act of 1966 generally reflect the merits and shortcomings of the Act as a whole. Whereas the impetus for

44) Op cit. supra footnote 37.

revision of the taxation of foreigners came from a desire to improve the balance of payments, the final provisions may not have that result. True, the rates have been reduced and the exemptions increased, but at the same time the basis of the taxable estate may be substantially increased by the provisions relating to the situs of bonds and bank deposits. Those revisions are certainly admirable in creating uniformity in tax treatment of various types of intangibles, but it is indeed questionable whether the net result of such provisions will be to encourage foreign investment in the U.S.

Moreover, the avoidance of U.S. estate taxes by the vehicle of a foreign holding company remains a possibility in the hands of a nonresident alien and to that extent U.S. estate taxes even if more liberal will continue to be a trap for unsophisticated (or unwealthy) foreign investors.

The provisions relating to expatriates are in some ways comparable to the Berlin wall and to the Cuban laws relating to refugees. If a citizen of the U.S. wants to leave the U.S. and give up his citizenship he may have to pay a substantial price to do so. The U.S. is apparently the only country which imposes tax by reason of citizenship even in the case of nonresidents, and it now appears that the U.S. will pursue nonresidents who are not citizens solely by virtue of the fact that such persons gave up their citizenship to reduce their taxes. Not only is the principal unhealthy, but the standards of judgment here will be difficult insofar as they are based on subjective motives of the expatriates. While the new provisions will make it less desirable to become an expatriate, it will encourage those intending to lose their citizenship to remove their assets from the U.S. and it is therefore questionable whether these provisions will have any effect or if so, whether that effect will not be negative.

The history of this Act also illustrates some of the peculiarities of the American legislative process which foreigners generally find so baffling. The Foreign Investors Tax Act was basically a very sound measure of a fairly noncontroversial nature, virtually assured of passage without difficulty. Due to that very fact, the measure became a sort of "Christmas tree" in its final form, carrying a grab bag of special interest measures. To defeat some of those riders to the Bill would have required defeat or at least substantial delay of the entire measure which nearly all agreed was for the most part a sound and desirable piece of legislation. It is doubtful whether many of the riders to the Bill could have passed on their own merits and at any time other than in the moments immediately prior to adjournment of Congress. At any rate it would appear that the riders attached to the Foreign Investors Tax Act did not receive sufficient legislative scrutiny and were not adequately exposed to public comments and suggestions. This, then, is somewhat less than the ideal conceptual basis of the legislative process as reflecting the desires of the people or at least the desires of their representatives.

A COMPARATIVE STUDY OF THE PRESENT PHILIPPINE TAX CODE AND THE PROPOSED TAX CODE*)

Commonwealth Act No. 466, otherwise known as the National Internal Revenue Code, has been in force since 1939. Since then, numerous rulings have been laid down interpreting its provisions. Novel problems have constantly arisen. A Tax Code enacted more than a quarter of a century ago cannot possibly cope with these legal problems and change of conditions. Hence, there is a need of updating our present Tax Code.

It is through the tireless effort of the Joint Legislative-Executive Tax Commission that a proposed tax code is made possible. It was introduced during the last regular session of Congress as H.B. No. 1310, in the Lower House by Congressmen Tan, Peralta, Roces and Tabios. An identical bill was introduced in the Senate. However, it was not approved. It is now under study by both Chambers of Congress.

It may be well to be apprised of the important innovations sought to be introduced by the proposed Tax Code for it will surely affect the activities of taxpayers. This is not, however, a guaranty that its provisions will remain unchanged in the process of legislation.

INCOME TAX

A *Tax on Individuals*

1. For citizens and residents of the Philippines, the graduated tax rates of 3% to 60% are increased from 5% to 65% for incomes ranging from not over P2,000**) to over P500,000.

There is also an increase in the income brackets. The tax rates for the lower and upper income brackets have been increased; that of the middle income brackets have been reduced. Its purpose is to set up a progressive individual income tax rate in order to increase revenue and contribute to the redistribution of income.

2. Nonresident aliens engaged in trade or business in the Philippines are subject to the graduated rates applicable to citizens and residents of the Philippines.

3. Nonresident aliens not engaged in trade or business in the Philippines are subject to a tax equal to 20% of their gross incomes. If their gross incomes exceed P23, 818, the graduated rates applicable to citizens and residents shall apply to them. But in no case the tax shall be less than 20% of their gross incomes.

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**) P: Philippine peso.

COMPARATIVE STUDY PHILIPPINE PRESENT AND PROPOSED TAX CODE

COMPARATIVE TABLE ON INDIVIDUAL INCOME TAX

Present Tax Code

Net Income Bracket	*Rate*
Not over P2,000	3%
Over P2,000 to P4,000	6%
Over P4,000 to P6,000	9%
Over P6,000 to P8,000	16%
Over P8,000 to P10,000	20%
Over P10,000 to P20,000	24%
Over P20,000 to P30,000	30%
Over P30,000 to P40,000	36%
Over P40,000 to P50,000	40%
Over P50,000 to P60,000	42%
Over P60,000 to P70,000	44%
Over P70,000 to P80,000	46%
Over P80,000 to P90,000	48%
Over P90,000 to P100,000	50%
Over P100,000 to P120,000	52%
Over P120,000 to P140,000	53%
Over P140,000 to P160,000	54%
Over P160,000 to P200,000	55%
Over P200,000 to P250,000	56%
Over P250,000 to P300,000	57%
Over P300,000 to P400,000	58%
Over P400,000 to P500,000	59%
Over P500,000	60%

Proposed Tax Code

Net Income Bracket	*Rate*
Not over P2,000	5%
Over P2,000 to P4,000	8%
Over P4,000 to P6,000	12%
Over P6,000 to P8,000	14%
Over P8,000 to P10,000	16%
Over P10,000 to P12,000	18%
Over P12,000 to P14,000	20%
Over P14,000 to P16,000	22%
Over P16,000 to P18,000	24%
Over P18,000 to P20,000	25%
Over P20,000 to P24,000	27%
Over P24,000 to P28,000	29%
Over P28,000 to P32,000	31%
Over P32,000 to P36,000	33%
Over P36,000 to P40,000	36%
Over P40,000 to P46,000	39%
Over P46,000 to P52,000	41%
Over P52,000 to P58,000	42%
Over P58,000 to P64,000	44%
Over P64,000 to P70,000	45%
Over P70,000 to P78,000	47%
Over P78,000 to P86,000	49%
Over P86,000 to P94,000	51%
Over P94,000 to P102,000	52%
Over P102,000 to P110,000	53%
Over P110,000 to P120,000	54%
Over P120,000 to P130,000	55%
Over P130,000 to P140,000	56%
Over P140,000 to P150,000	57%
Over P150,000 to P160,000	58%
Over P160,000 to P180,000	59%
Over P180,000 to P200,000	60%
Over P200,000 to P250,000	61%
Over P250,000 to P300,000	62%
Over P300,000 to P400,000	63%
Over P400,000 to P500,000	64%
Over P500,000	65%

B *Tax on Corporations*

1. Domestic Corporations—The tax rate is increased from 22% to 25% for corporations whose net incomes do not exceed P100,000. For corporations whose net incomes exceed P100,000, the tax rate is increased from 30% to 33%.

2. Foreign Corporations—Resident foreign corporations engaged in trade or business in the Philippines are subject to the same rates imposed upon domestic corporations. For nonresident foreign corporations not engaged in trade or business in the Philippines, the tax rate is increased from 30% to 33% of their gross incomes in the Philippines.

C *Tax on Special Types of Corporations and Institutions*

1. Insurance Companies
   (a) Domestic and foreign life insurance companies are at present subject to a 6 1/2% tax on their net investment incomes. It is proposed to subject them to the same 25% and 33% rates imposed on other kinds of corporations based on their net investment incomes.
   (b) Foreign life insurance companies not doing business in the Philippines are subject to a 33% tax on their gross investment incomes received from all sources within the Philippines.

2. Educational institutions, whether sectarian or nonsectarian, shall pay a tax of 10% of their taxable net incomes. Under the present law only nonsectarian educational institutions are liable to the 10% flat rate. Sectarian educational institutions enjoy full exemption under Section 27(e) of the Tax Code. The deletion of the word "educational" in the said section would make them liable to the 10% flat rate on their net income.

D *Withholding Tax*

1. In the case of nonresident aliens not engaged in trade or business in the Philippines, the withholding tax is increased from 20% to 30% of their incomes consisting of interests, dividends, rents, salaries, premiums, annuities, and the like received in the Philippines.

2. For foreign corporations not engaged in trade or business in the Philippines, the withholding tax is increased from 30% to 33% of the incomes received in the Philippines, consisting of interests, premiums, rents, annuities and the like. However, they need not report 15% of dividends received from domestic corporations which are themselves subject to tax.

E *Exemption Granted to Estates and Trusts Withdrawn*

The present exemption of P1,800 granted to estates and trusts is withdrawn. The reason given for the withdrawal is that personal exemptions are granted to individual taxpayers as a matter of equity, representing an arbitrary amount to cover personal, living and

family expenses, which are nondeductible. By their nature, estates and trusts do not incur personal, living and family expenses.

F *Exemptions on Corporations*

1. Dividends received by domestic or resident foreign corporations from domestic corporations subject to income tax are exempt to the extent of 75% thereof. In the case of nonresident foreign corporations, the extent of exemption is 15%.

2. There is a withdrawal of exemption granted under the present Section 27(i) of the Tax Code to mutual or cooperative telephone companies. The reason given is that telephone companies do not have the same nature as typhoon or fire insurance companies, or ditch or irrigation companies.

G *Deductions from Gross Income*

1. Entertainment expenses are deductible to the extent of 10% in the case of an individual, or 5% in the case of a corporation, from his or its gross income. To be deductible, it must be substantiated by appropriate proofs, except when it does not exceed P100. However, entertainment expenses incurred for government officials and employees are not allowed to be deducted.

Nonresident aliens and foreign corporations are entitled to deduct only such necessary expenses incurred in carrying on any business or trade in the Philippines exclusively. Hence, nonresident aliens or foreign corporations not engaged in trade or business in the Philippines are not allowed this deduction.

2. Interest paid on delinquency or deficiency in the payment of any tax may not be claimed as a deduction.

3. Any tax on income imposed by a foreign country shall be deductible only if the tax is imposed on income derived from that country, provided the taxpayer has not signified in his return the desire to claim a tax credit. The reason given is to avoid the injustice in a situation where the Philippines will have to allow the deduction of taxes imposed by a foreign country on income earned in the Philippines by a taxpayer who happens to be a national of that foreign country.

A foreign tax credit may not, however, be claimed if the taxpayer elects the optional standard deduction.

4. Casualty losses are deductible only if the value of the property lost exceeds P500. This is to restrict the deduction of nominal amounts of casualty losses which are difficult to check.

5. Bad debts are limited only to business bad debts. This is to avoid erosion of the tax base through the deduction of an item which is difficult to check.

6. Allowance for depreciation or obsolescence is limited only to property used in the trade or business, or property held for the production of income. No deduction is allowed for its non-use, as under the present Tax Code.

There are two methods of computing depreciation allowance: (a) the straight line, and (b) the declining balance method, at a rate not exceeding twice the rate of annual allowance computed under the straight line method. This is to set up a definite method of

computing depreciation in order to remove from the Commissioner the power to decide what method is reasonable for each taxpayer.

The declining balance method shall apply only to tangible property but only if the property is used in manufacturing, production, extraction, or of furnishing transportation, communication, electrical energy or constitutes storage facility used in connection with any of the activities herein mentioned.

7. Net Operating Loss—The proposed Tax Code allows as a deduction an amount equal to the aggregate of the net operating loss carryover. A net operating loss for any taxable year ending after December 31, 1966 shall be carried over to each of the five taxable years following the taxable year of the loss. A net operating loss is to be determined without taking into account the net operating loss for any prior year. It is the excess of the deductions allowed over the gross income. The excess shall be computed with the following adjustment:

Gross income plus—

Tax exempt income or partially excluded income or both; add back deductions otherwise allowed by law not attributable to the operation of a trade or business regularly carried on by the taxpayer

H *Optional Standard Deduction*

The proposed Tax Code clarifies the present law by providing that, in lieu of the itemized deductions, an individual, other than a nonresident alien *not engaged in trade or business* in the Philippines, may elect a standard deduction. It shall be in the amount of P1,000 or 10% of his gross income, whichever is less. Nonresident aliens not engaged in trade or business in the Philippines are not allowed deductions, as they are taxed on the basis of their gross income.

I *Change in Accounting Period*

If a taxpayer, other than an individual, changes its accounting period, the taxable net income for the short period is annualized and on the basis of which the income tax is apportioned to the short period. The taxpayer shall also file a separate return for the period covering the start of the new accounting year and the date the old period would have terminated, and the tax for the short period shall be adjusted accordingly. Under the present law, the return for the short period is based on the taxable net income for the short period and remains undisturbed.

J *Deficiency Interest*

The period for which interest may accrue on a deficiency assessment (6% a year and 12% if unpaid when due) is extended from 3 to 5 years.

K *Extension to File Return*

Under the proposed Tax Code, when a taxpayer has been granted an extension of time

for filing a return, interest runs at 6% (presently 12%) a year from the original due date to the time of payment. If no extension has been granted, interest rate remains at 12% per annum.

ESTATE TAX

A *Minimum Taxable Amount Increased; Inheritance Tax Abolished*

The minimum taxable amount is increased from over P5,000 to not over P10,000. The tax rates of from 1% to 15% are increased from 3% to 37%. The increase is primarily due to the proposed abolition of the inheritance tax, the present rates of which are 2% to 22%. The estate brackets are increased. This is to redistribute wealth on a wider scale.

Proposed Estate Tax Rates

Taxable Estate	*Amount*	plus	*On Excess*
Not over P10,000	3%		
Over P10,000 to P20,000	P300		5%
Over P20,000 to P30,000	P800		7%
Over P30,000 to P50,0000	P1,500		9%
Over P50,000 to P75,000	P3,300		11%
Over P75,000 to P100,000	P6,050		14%
Over P100,000 to P150,000	P9,550		17%
Over P150,000 to P200,000	P18,050		20%
Over P200,000 to P250,000	P28,050		23%
Over P250,000 to P350,000	P39,550		26%
Over P350,000 to P500,000	P65,550		29%
Over P500,000 to P750,000	P109,050		32%
Over P750,000 to P1,000,000	P189,050		35%
Over P1,000,000	P276,550		37%

B *Estate Tax Exemption Increased*

The estate tax exemption is increased from P5,000 to P10,000. The bill states that one of the primordial objectives of estate taxation is to redistribute wealth on a wider scale. If a small estate of P10,000 or less is further diminished by taxation, then it would not be in accord with the spirit of redistribution.

C *Reciprocity Provision Withdrawn*

The provision granting reciprocal exemption from estate and inheritance taxes to non-resident aliens of the Philippines is withdrawn. If the benefits of reciprocity are later found desirable, the suggestion is made to secure these benefits through a tax convention with the proper country.

D *Limited Deduction for Charitable Transfers of Property at Death*

Under the present law, there is no deduction allowed for transfers of property at death in favor of charitable institutions. On the other hand, transfers by gift to these institutions are entitled to exemption under the gift tax provision. The proposed Tax Code allows a deduction of not exceeding 20% of the decedent's gross estate for transfers of property through inheritance in favor of domestic charitable institutions.

GIFT TAX

A *Donee's Tax is Abolished*

Under the proposed Tax Code, the donee's tax is abolished. The present method of taxing transfers of property by gift is complicated. It is requires a computation of taxes on all previous gifts by the donor and on gifts received by the donee from all sources. This double computation imposes a heavy burden on both the tax collecting agency and the taxpayer. So it is proposed to discard the donee's tax to simplify procedure.

B *Donor's Gift Tax*

1. Minimum taxable amount increased—The minimum taxable amount is increased from over P5,000 to not over P10,000. The gift brackets are increased. The tax rates of from 1% to 15% are increased from 3% to 37%. The tax brackets and rates of the proposed estate and gift taxes are the same.

2. Donor's annual exemption of P1,000—The proposed Tax Code provides for an annual exemption of P1,000 in favor of donors. It recognizes Philippine liberality of giving small gifts to loved ones on Christmas, birthdays, anniversaries and the like. It will do away with the present method of keeping records even of small gifts.

3. Donor's specific lifetime exemption increased—The donor's specific lifetime exemption is proposed to be increased from P5,000 to P10,000. It is categorized as a deductible item. In this way, it will be reflected in the returns. The tax collecting agency will have on record all previous gifts of the donor for the purpose of computing the cumulative tax on all gifts.

Any gift made in excess of the donor's annual exemption of P1,000 shall be offset against his specific lifetime exemption.

PRIVILEGE TAX ON BUSINESS

A *Metropolitan Manila Defined*

Metropolitan Manila includes the City of Manila, Quezon City, Pasay City, Caloocan City and the Municipalities of San Juan, Mandaluyong, Makati, Parañaque, Navotas and

Malabon. This definition is made necessary in view of the fact that the tax rates on business and occupation are highest in Metropolitan Manila, higher in other chartered cities and provincial capitals, and lower in all other places.

B *Classification of Businesses Subject to Privilege Tax*

1. Those dealing in commodities subject to specific tax;
2. Those subject to miscellaneous excise taxes; and
3. Those not included in the first and second categories which generally pay only the fixed tax.

C *Manufacturers, Importers, Exporters and Dealers of Commodities Subject to Specific Tax*

1. Guidelines for their reclassification and readjustment of rates are the following:

(a) Imposition of relatively higher privilege tax on alcoholic beverages is primarily sumptuary in purpose. There is an increment of tax on distilleries, compounders, repackers and rectifiers, and on certain dealers and peddlers of alcoholic beverages.

(b) At present peddlers or dealers of wines are treated for tax purposes equally with peddlers or dealers in distilled spirits. Since the alcohol content of wines approximates that of fermented liquors, they should be taxed at the same rate. Distilled spirits have a higher alcohol content, so a higher tax is imposed on peddlers and dealers of these items than those handling fermented liquors and wines.

(c) Higher taxes are imposed on wholesalers than on retailers. It is recognized that there is a disparity in their volume of business, capitalization and profitability.

(d) The tax rates of peddlers and dealers are made identical.

(e) Majority of persons manufacturing or dealing in commodities subject to specific tax pay a privilege tax at varying rates. Others pay only the specific tax. It is proposed likewise to subject the latter group, comprised of manufacturers or importers of matches, firecrackers, petroleum products, playing cards and saccharine, to a privilege tax on business. This will place all businesses liable to specific tax on the same footing.

D *Business Subject to Miscellaneous Excise Taxes*

1. The privilege tax imposed on this class of business is increased. The privilege tax on manufacturers, producers, exporters, millers, contractors, caterers and transport operators has been increased from P20 to P50.

2. Exporters of embroideries and wearing apparel and publishers are liable to the privilege tax, in spite of the fact that they are exempt from the contractors tax under Section 191 of the present Tax Code.

3. Banks, finance, investment and insurance companies doing business in the Philippines are liable to a privilege tax of P500 in Metropolitan Manila, P250 in other chartered cities and provincial capitals, and P150 in other places. Under the present law, they are

liable only to a miscellaneous excise tax. The proposal seeks to place them on an equal footing with other businesses subject to the privilege tax.

E *All Other Businesses*

On all other businesses, the privilege tax is imposed on their gross annual sales or receipts during the preceding calendar year. The rates are increased and made proportional, in view of the fact that they are not liable to any other business tax.

PRIVILEGE TAX ON OCCUPATION

A *Inclusion of a Number of Occupations and Professions Subject to the Tax*

A certain number of persons performing specialized occupations have lately had high earning potentials but are not taxed. They include movie directors, actuaries, public relations and advertising men, management and investment consultants, radio and television announcers, nutritionists and interior decorators. It is proposed to tax them to promote greater equity.

B *Increase in the Number of Tax Rates*

The number of rates has been expanded from two (P75 and P50) to five (P80, P60, P40, P20 and P10). This is accompanied by a reclassification of occupations and professions so as to place those which have generally high earning capacities under the upper tax categories and those which are less lucrative within the lower scale.

C *Individuals Engaged in Two or More Allied or Related Occupations or Professions*

Individuals engaged in two or more allied or related occupations or professions are subject to only one tax. If the rates on these professions or occupations are not of the same amount, the individual concerned shall pay the higher or highest rate, as the case may be. This is intended to avoid double taxation.

D *Local Governments Can Tax Persons Subject to Annual Privilege Tax on Occupation*

Under the proposed Tax Code, a person authorized to practice his profession or occupation, who has paid the corresponding annual privilege tax on occupation, shall be entitled to practice his occupation in any part of the Philippines without being subject to any other national tax, charge, license or fee for the practice of his profession or occupation.

This would enable local governments to exercise their powers under Section 2 of the Local Autonomy Act. It is also in line with Section 179 of the present Tax Code, wherein it is provided that the payment of a business or occupation tax shall not prohibit any

municipality from placing a tax upon the same business or occupation for local purposes, where the imposition of such tax is authorized by law.

E *Liability of Employers for Employees Who Have Not Paid the Privilege Tax on Occupation*

Any person or corporation employing a person subject to the privilege tax on occupation shall require payment by that person of the privilege tax on occupation before employment and annually thereafter. Failure of the employer to discharge this duty shall subject him, in case of an individual to fine or imprisonment or both, and in the case of a corporation, to a higher fine.

However, the exemption from occupation tax remains in the case of any professional employed and performing duties in his professional capacity but without permission to practice his profession during or after office hours to private or personal clientele.

SPECIFIC TAXES

1. The tax on some of the articles or commodities subject to specific tax is increased, such as distilled spirits, beer, cigarettes, fireworks, lubricating oil, naphtha, including lighter fluids, gasoline, denatured alcohol for motive power, bunker oil. One of the reasons for the increase in tax is to discourage consumption of these articles.

2. Others are subject to the same rate, such as wines, cigars, matches, kerosene, coal, coke, cine films, saccharine and sodium saccharinate.

3. The rest have reduced rates, such as playing cards. The reason given for the reduction of the tax on playing cards is to minimize smuggling of these articles.

4. Domestic denatured alcohol used for any purpose other than for motive power is exempt from specific tax. Its purpose is to grant appropriate business incentives to local industries.

Comparative Table of Rates on Specific Taxes

Articles or Commodities	*Present*	*Proposed*
Distilled spirits, per proof liter	P0.70-P15.00	P0.85-P17.00
Wines, per liter	P1.00-P12.00	P1.00-P12.00
Fermented liquors, per liter	P0.25	P0.40
Flavoring extracts, per liter	P0.70-P15.00	P10.00
Cigars, per thousand	P2.30-P7.00	P2.30-P7.00
Cigarettes, per thousand	P2.50-P24.00	P2.50-P18.00
Other manufactured products of tobacco, per kilogram	P0.75	P0.75
Tobacco specially prepared for chewing, per kilogram	P0.60	P0.60
Matches, per gross of 80-stick boxes	P0.50	P0.50

Articles or Commodities	*Present*	*Proposed*
Fireworks, per kilogram	P20.00	P10.00-P20.00
Kerosene and Liquefied Petroleum Gas, per liter	Po.025	Po.025
Lubricating oils, per liter	Po.07	Po.08
Naphtha, including lighter fluid, gasoline, and similar products, per liter	Po.08	Po.10-0.12
Denatured alcohol for motive power, per liter	Po.01	Po.04
Bunker oil and similar fuel oils, per ton	Po.40	P10.60-P21.20
Diesel oil and similar oils	P1.00 per ton	P.002-Po.04 per liter
Coal and Coke, per ton	Po.25	Po.25
Cinematographic films, including those for television, per meter	Po.15-Po.20	Po.15-Po.20
Playing cards, per pack of 60 cards	P10.00	P5.00
Saccharine and Sodium Saccharinate, per kilogram	P75.00	P75.00

Sodium saccharinate is presently subject to 7% sales tax. It is proposed to subject it to specific tax in the same way as saccharine.

PERCENTAGE TAXES ON COMMODITIES

A *Change in the Manner of Computing the Sales Tax on Domestic Manufacture*

Under the present system, the sales tax is computed on the basis of gross selling price after deducting the cost of raw material used in the manufacture of finished products. The cost of raw material is allowed as deduction only if it had been previously taxed at the same rate as the finished article, with certain exceptions. This is double taxation.

The proposal is to introduce another method in order to minimize double or multiple taxation. It involves the computation of the tax on the basis of gross sales without allowance on previously taxed raw materials. Against the tax so computed would be credited any sales and millers tax actually paid on account of raw materials, regardless of the rate to which such raw materials are subjected. Deduction of the tax should be allowed only if the amount of the tax is shown as a separate item in the purchase invoice of the raw materials.

B *Percentage Tax on Automobiles*

Under the proposed Tax Code, the percentage tax for domestically manufactured or assembled automobile is based on its selling price. It is unlike the present system where the tax is dependent on the ratio of raw material component to the total cost. The greater the ratio, the lower is the effective rate: conversely the smaller is this ratio, the higher is the effective rate.

Hence, the price bracketing is updated as a basis for rate differentiation. The tax on automobile is progressive, with effective rates on lower priced cars than on more expensive ones. The tax will vary with the price, not with the material component of the automobile. This will eliminate the discriminatory treatment against domestic cost component.

The minimum gross value of an automobile subject to tax is increased from not in excess of P7,000 to not in excess of P10,000. There is hardly any brand new car which currently sells for less than P7,000.

1. Present schedule of sales tax on automobiles

Selling Price	*Rate*
Not exceeding P7,000	50%
Over P7,000 to P10,000	75%
Over P10,000	100%

The tax base for imported automobiles is landed cost plus 100%.

2. Proposed schedule of sales tax on domestically manufactured or assembled automobiles

Gross Value	*Amount* plus	*On Excess*
Not exceeding P10,000	10%	
Over P10,000 to P12,500	P1,000	15%
Over P12,500 to P15,000	P1,375	20%
Over P15,000 to P20,000	P1,875	30%
Over P20,000	P3,375	50%

There is no reference to imported automobiles in the proposed Tax Code. Parts and accessories as replacements or as completely knockdown parts for assembly are taxed at 7%. If imported, the markup is 25% as under the present Tax Code.

C *Percentage Tax on Other Articles*

1. Toilet preparations—It is reduced from 50% to 7%. The justification for the reduction is that they are widely consumed by those who belong to the low income brackets.
2. Luggage and similar articles—It is reduced from 30% to 15%.
3. Industrial clocks—It is reduced from 30% to 7%.
4. For ordinary watches, from 30% to 7%.
5. Phonographs, radios and television—It is increased from 7% to 15%. The reason given is that most of the purchasers are the middle and upper income groups. The increase is based on the ability to pay principle.
6. For tape recorders, it is increased to 30%.
7. For phonograph records, it is reduced to 7%.

8. For pianos, it is reduced from 30% to 15%. This will be an incentive to local manufacturers using local materials and help develop the skill of our local craftsmen.
9. For phonographic equipment and films, it is reduced to 15%. This is to alleviate the heavy cost of procurement of these items and help the local movie industry.
10. For photostatic copying machine and other cameras and machines for photographing or copying documents, it is reduced from 30% to 15%.
11. For locally made electric fans, it is reduced from 30% to 15%.
12. For cooking appliances with oven, 15%.
13. For ordinary cooking stoves, 7%.
14. Republic Act No. 3029 reduced the tax rate on refrigerators, airconditioners and similar items from 30% to 15% and 7% for those which are locally manufactured by nonintegrated and integrated firms, respectively. It is proposed to set up a tax of 10% on integrated product and 15% on nonintegrated product.
15. For synthetic fabrics and manufactures thereof, 15%.

D *Sales Tax Exemption Granted to Agricultural Products Restricted*

The sales tax exemption granted to agricultural products is restricted. The exemption applies only to domestic agricultural products and ordinary salt when sold, bartered, or exchanged in their *original form* by a producer or owner of the land where produced, as well as all kinds of fish in their original state. Agricultural products exclude those which have undergone processing or manufacturing as defined in this Code, except copra, stripped or unstripped fibers and other agricultural products subjected to the mere process of cutting, smoking, drying, freezing or salting.

The amendment is made necessary in order to remove the inequity where a producer who processes or cans the agricultural products he raises is not liable to the sales tax, while the one who does not grow his own raw materials is subject to the sales tax.

E *Restriction Limiting Sales Tax Exemption on Exports made by Manufacturer or Producer Removed*

The restriction limiting sales tax exemption on exports only to those effected by the manufacturer or producer is removed. Any subject articles exported, either for sale or consignment, are exempt irrespective of who is the exporter.

F *Coconut Coir, Dessicated Factories and Sugar Mills Run by Any Power Other Than Man or Animal Power Subject to 2% Millers Tax*

Coconut coir or fiber, dessicated factories and sugar mills run by any power other than man or animal power are subject to a millers tax of 2% of the gross value of their output.

G *Exemption from Compensating Tax*

Vessels imported by a Philippine citizen, partnership, association, or corporation organized

under Philippine laws and duly licensed to engaged in coastwise or overseas shipping business or in the construction of vessels for such purpose are exempt from the payment of compensating tax. However, it is necessary that a previous certification is obtained from the National Shipyard and Steel Corporation that the vessel or parts thereof sought to be imported cannot be procured locally at a reasonable price.

PERCENTAGE TAX ON SERVICES

1. The tax on cockpits, night and day clubs and cabarets is increased from 10% to 20% of their gross receipts. This is a means of social control. By discouraging patronage, available financial resources would be channeled to more productive endeavors.

2. Establishments maintained or operated by clubs of any kind or nature, selling or catering exclusively to members thereof or their guests, shall be liable to a 20% tax based on their gross receipts.

3. Transport operators subject to the franchise tax and jeepney operators are exempt from the 2% transport tax.

TAX ON FINANCE AND INVESTMENT COMPANIES

Finance and investment companies doing business in the Philippines are subject to a tax of 3% of their gross receipts, derived from interests, discounts, dividends, commissions, profits from exchange, royalties, rentals from property and all other items treated as gross income.

Under present law, they are not subject to any business tax except a nominal privilege tax. Other financial institutions, such as banks and insurance companies, are subject to business tax. The justification given is that the business of financing and investment has become profitable and that it would be unfair not to tax them.

FRANCHISE TAX

5% Franchise Tax Based Soley on Gross Earnings from the Business

The franchise tax of 5% imposed upon the business covered by the franchise is based solely upon its gross earnings. It is no longer based on its gross earnings or receipts. This is made possible by the deletion of the word "receipts". Gross earnings would include accrued amounts although not actually received.

The reason given for the deletion is that collection of earnings properly pertains to the franchise grantees and there is no justification why taxes on said accrued earnings have to be postponed simply because franchise holders are inefficient in their collection of fees for services already rendered.

AMUSEMENT TAXES

1. The tax on cockpits, cabarets and day and night clubs is increased from 10% to 20% of their gross receipts.

2. Jai Alai and race tracks are also subject to a 20% tax on their gross receipts.

3. The exemption of admission fees of Po.20 or less is withdrawn. It was noted that the splitting of admission fees into Po.20 denominations to evade the tax has been widespread, especially in the provinces. The minimum amount of a tax on admission fees of Po.20 or less will close the avenue for tax evasion.

4. The partial exemption of boxing exhibition is reduced from 50% to 20% of the rates of the tax on admission. The present exemption is no longer warranted in view of the popularity and profitability of boxing.

5. Exemption of operas, concerts, recitals, etc., as provided in Republic Act No. 722 and now incorporated in the present Tax Code, is proposed to include ballet among those exempt.

6. The 50% amusement tax exemption granted to charitable benefits is qualified to the extent that the amount accruing to the charitable institution concerned must be at least equal to the taxes waived by the government, plus 35% of the net profits. This is to remedy the abuses committed by promoters of pocketing the profits while charitable institutions receive only a small portion of the proceeds.

DOCUMENTARY STAMP TAX

A *On Leases or Other Hiring Agreements*

The stamp tax on leases or other hiring agreements has been increased from Po.60 to P1.00, if excuted for not more than one year; P1.50 to P2.00 if more than one year but less than three years; and, from P3.00 to P4.00 if more than three years.

B *On Mortgages or Deeds of Trust*

When the amount for which the mortgage or deed of trust is given exceeds P500 and does not exceed P3,000, P1.50. This amendment seeks to subject transactions involving P500, rather than exempt it from this tax rate and tax it under the general provision at Po.30.

C *On Sale or Conveyance of Real Property*

Under the present law, when the amount of the consideration in sale or other conveyance of real property exceeds P200 but does not exceed P1,000, the tax is Po.75. The proposal seeks to impose the tax when the amount of the consideration does not exceed P1,000. It removes the tax exemption aspect when the amount of the consideration is P200 or less.

MISCELLANEOUS TAXES

A *On Sealing of Weights and Measures*

The fees for sealing of weights and measures have been increased. The present fees could hardly cover expenses in their collection.

B *On Firearms*

1. Holders of caliber 22 firearms, including low-powered rifles, are required to pay the initial and annual license fees. This type of rifle is destructive to life and limb as other firearms subject to the firearms tax.

2. The proviso of Section 292 of the Tax Code imposing upon members of duly organized gun clubs a lower rate of initial and annual license fees for each firearm is deleted.

3. Hunting permit fee is increased from P2.00 to P20.00.

C *On Tax Clearance Certificates*

1. For departing individuals, the fee is increased from P15.00 to P30.00, in the case of first class passenger; from P8.00 to P16.00, in the case of second or tourist class passenger; and from P2.00 to P4.00, in the case of a third class or steerage passenger.

2. For the issuance of any other tax clearance certificate, P5.00.

D *Mining Taxes*

1. The annual occupation fee for any mining claim is increased from P1.00 to P2.00 per hectare to cover administrative costs.

2. The rentals and royalties on mineral lands under lease have been increased, considering that the prices of mine products have increased yearly.

3. The *ad valorem* tax is increased from 1 1/2% to 3% of the actual market value of the annual gross output of the minerals or mineral products extracted or produced from all mineral lands not covered by lease.

4. Minerals subject to *ad valorem* tax are entitled to a 5% deduction of the amount due from the government. This is the same privilege granted by the present law on minerals mined on private land subject to royalties.

E *Charges on Forest Products*

1. Charges on timber cut in public forest reserves are increased by 25%. The rising prices of logs and their manufactures justify the increase.

2. A miner or mining company must first secure a license to cut timber in his or its mining claim before he or it could do so in the development of such mineral claim. Otherwise, he or it would be liable to the penalties, delinquencies and surcharges imposed by law for illegal cutting and removal of forest products. The purpose is to curtail indiscriminate logging activities in mineral lands, which could have the same detrimental consequences as illegal cutting of timber from forest lands.

G. L. BORG:

THE ASSESSMENT SECTION IN THE MALTA INLAND REVENUE DEPARTMENT

Most of the activities of the Inland Revenue Department are in the form of applying the law relating to the imposition of taxes and the collection of revenue.

The authority to assess and collect income tax in the Maltese Islands is derived from the Income Tax Act.[1]) *To the Commissioner of Inland Revenue was entrusted the task of managing the Act. Thus he was given the authority to assess and collect Income Tax. The powers conferred and the duties imposed by the Act upon the Commissioner of Inland Revenue may be performed by him personally or by any other officer under his control as delegated by him. Thus the Inland Revenue Department was constituted by an Act of Parliament and started operating in August 1948 to assist the Commissioner in executing the task afforded him*[2]).

In this article, the powers that the law has given to the person to whom it has entrusted the various steps in the process of determining income tax liabilities or the regulation of procedure has been reviewed.

The Act enjoins the Commissioner to search for income wherever it is found. The income-tax assessment proceedings commence with the issue of a notice in writing. In fact, the Act empowers the Commissioner, by notice in writing, to require any person or body of persons to furnish him, within a reasonable time not being less than thirty days as may be specified in the notice a return of income and such particulars as may be required with respect to such income[3]).

When the Commissioner has reasons to believe that a person or persons may leave the Island without having submitted a return, the minimum period of thirty days is not insisted upon by the Act and the Commissioner of Inland Revenue may require such person or persons to furnish a return of total income or other particulars relating to such income within any time specified in the notice.[4])

The Act does not prescribe on which day or month the Commissioner is to serve returns on taxpayers but normally the despatch of notices is expected to be executed during the first three months of the year of assessment. The onus to furnish a return of total income is on the taxpayer and he will not be relieved from any penalty on the grounds that a notice had not been served upon him or that the prescribed form had not been delivered to him. The Commissioner normally forwards returns to the majority of taxpayers. However, when any person chargeable with tax has not received a

1) Act No. LIV of 1948 as amended by Act No. VI/1953, Act No. XX/1955, Act No. V/1958, Ordinance No. XVI/1959, Ordinance No. XXV/1960 and Ordinance No. XXIV/1961.
2) Government Notice No. 497/1948.
3) Income Tax Act, 1948, section 37 (1). Vide specimen Income Tax Return Forms (Appendices No. 8 to 12).
4) Income Tax Act, 1948, section 65 (2) (a).

return before the 30th June in any year he shall be bound to give notice himself to the Commissioner that he is so chargeable before the 31st July of that same year.[5])

Taking advantage of the failure on the part of the Income Tax Act to impose a period within which notices are to be sent by him to taxpayers for the furnishing of returns, the Commissioner may require any person to render an interim return in cases inter alia where a taxpayer dies or leaves the Island for good or becomes insolvent during the year immediately preceding the year of assessment (basis year).

The Commissioner may, when and as often as he thinks necessary, require any person to make further or more detailed returns respecting any matter of which a return is required or prescribed by the Income Tax Act. If the Commissioner is not satisfied with the contents of a return that has been furnished or feels that further returns or statements are necessary, he may serve on such person a notice requiring him to attend personally or by representative at his Office or to produce or to cause to be there produced any evidence on which such person may rely in support of the return, including trade books, bank books and bank statements.[6])

In Malta, there is no time limit prescribed by law as to for how long a period the Commissioner may retain books and other documents in his possession prior to assessment. Restriction of time is only provided in the Act in the case when trade books or other documents are seized from outside the office of Inland Revenue against the will of the taxpayer.[7])

The powers of the Commissioner extend also over other Heads of Departments in as much as he may require any civil servant to supply information and particulars which may be in his possession if such information is deemed to be necessary for the purposes of the Income Tax Act. However, such officer is not debarred from refusing to disclose any information or evidence at his disposal as to which he is under any statutory obligation to observe secrecy.[8]) The Secretary of the War Damage Commission, for instance, is precluded by the War Damage Ordinance from divulging information as to the amount of compensation granted to any person in respect of buildings demolished or damaged by enemy action.

In terms of Office Circular No. 43 of the 16 April 1960, assessing officers have been instructed to record on files and to report cases where taxpayers have failed to keep proper or sufficient records of income and expenditure to enable the Commissioner to ascertain his income and allowable deductions. Section 42 prescribes the keeping of

5) Income Tax Act, 1948, section 37 (2).

6) Income Tax Act, 1948, sections 38 and 39.

7) Income Tax Act, 1948, section 43 (1). In the Indian case "Pragdas Mathuradas vs Income Tax Officer" decided in 1950 (I.T.R. 757 761), it was held that the Indian Income Tax Authorities had no power to detain books of account produced before them. However, the ruling has now been rendered obsolete by the amendment in 1953 of section 37 of the Indian Income Tax Act, 1922. The amendment now brings the Indian Act in line with the Maltese counterpart law giving powers to certain Officers of the Department to impound and retain in their custody for such period as they think fit any books of account or other documents produced before them in any proceeding. Thus, in India, like Malta, there is no limit to the period for which the retention may continue. (Kanga & Palkhivala, The Law and Practice of Income Tax, page 815).

8) Income Tax Act, 1948, section 41.

records but does not specify the method or the language in which Accounts should be kept. Thus it is in the discretion of the Commissioner to ascertain whether a taxpayer has fulfilled the requirements of this section or not. When the Income Tax Bill was being discussed by the Legislative Assembly, clause 42 originally provided that proper and sufficient records should be kept in either the English or Maltese Language. An amendment moved by the Deputy Leader of the Opposition, Dr. G. Borg Olivier, cancelling the language requirement was agreed to by the House nem. con.[9]) and now Assessing Officers may be confronted with Trade Books that are kept in Italian or one of the Indian languages. Recently, an assessor dealing with the return of a member of the Indian Business community was faced with the difficulty of being presented by trade books kept in the Indian Language, which he had to accept. The veracity of the books had to be tested in a round-about manner to the satisfaction of the Commissioner, who it must be said is not entitled to insist that a qualified person keeps the books and prepares the accounts of a taxpayer.

On conviction, taxpayers who are found guilty to have contravened the law in not keeping proper records are liable to a fine of between twenty-five pounds and five hundred pounds.[10])

Trade Books are to be retained by taxpayers for a period of at least seven years after the completion of the transactions to which they relate. At any time during this period the Commissioner is empowered to require taxpayers to produce for examination, inter alia, any books, accounts, trade lists, stock lists or documents.[11])

The Malta Act does not require the preservation of records in the case of a company or a partnership which had gone into liquidation and which has been finally dissolved.[12]) In all other cases, unless authorised by the Commissioner, in writing, that their preservation is not required,[13]) all records are to be retained in their original form. In South Africa, it is expressly provided in the law that a taxpayer may, with the approval of the Commissioner, retain a micro-film copy in lieu of the original copy of any book or document. However, this concession is not granted in the case of any ledgers, cash books and journals.[14])

The Commissioner has the power to have at all times full and free access to buildings, places, books or other documents for any of the purposes of the Act and for that purpose may make extracts from or copies of any such books or other documents.[15]) Besides these extensive powers, the Commissioner may also seize and retain for such time only as may be absolutely essential and no longer, any books or documents which in his opinion furnish indispensable evidence of any offence against the Income Tax Act.

9) Official Report of the Debates of the Legislative Assembly, Second Session—First Legislature—Sitting No. 67, page 3491.
10) Income Tax Act, 1948, section 42 (3).
11) Income Tax Act, 1948, section 42 (1).
12) Income Tax Act, 1948, section 42 (2) (b).
13) Income Tax Act, 1948, section 42 (2) (a).
14) South African Income Tax Act, 1941, section 63 (i) (f).
15) Income Tax Act, 1948, section 43 (1). Vide also Appendix No. 5.—Copy of Authorization Certificate handed to Assessing Officers for the purposes of carrying out inspections outside the Office of Inland Revenue.

The Income Tax Bill was amended on a motion tabled by the Minister of Finance, thereby restricting the 'dictatorial' powers of the Commissioner to retain books in his possession for an indefinite period.[16])

The Commissioner is debarred, however, from seizing any Notarial Act or Register and inspecting public wills without the permission of the testators.[17])

Clause 43 of the Income Tax Bill gave rise to a lengthy discussion in the Legislative Assembly as regards the powers of the Commissioner to inspect treasure boxes (casse ignote) deposited at Banks which are suspected to contain interest bearing coupons and other documents respecting any undisclosed income. A member of the opposition benches, Dr. G. Pace, moved an amendment thereby trying to exclude the Banks from the obligation of allowing the Commissioner to get information from them, when the giving of such information is deemed to clash with the Banks' requirements of preserving secrecy with regards to banking transactions of depositors. The motion was negatived by the House and the Commissioner's powers to have full and free access to all buildings and places, as the law now stands, includes also, by all means, Banking Businesses and Banks.

In the United Kingdom, the Board of Inland Revenue itself has not the power to examine trade books or other documents outside the Departmental precincts. The Inspector of Taxes has not access to the books of account of the client[18]) However, failure on the part of a taxpayer to comply with the requirements of the Inspector as to the production of Trade Books, stock-sheets and other documents containing information as to transactions of the trade would involve a liability to a penalty; and in the case of a body corporate this liability extends not only to the body corporate itself, but also to the Secretary of the Company or his locum-tenens.[19])

In Malta, any person who fails to comply with the requirements of a notice given to him by the Commissioner under the Income Tax Act or who fails to attend at the Office of Inland Revenue or having attended, fails to answer questions lawfully put to him shall be guilty of an offence and shall be liable, on conviction, to a fine of between ten pounds and fifty pounds and a further fine of not more than two pounds for every day during which the default continues.[20])

Any person who, with intent to evade or to assist any other person to evade taxation, makes an incorrect return or gives incorrect information to any matter relating to assessment, shall be liable, on conviction, to very heavy penalties. Furthermore, if any person prepares or maintains or authorizes the preparation or maintenance of any false books of account or other records shall also be liable, on conviction, for heavy fines or imprisonment or to both fine and imprisonment. In both cases, the Commissioner is empowered to compound any offence and may before judgment stay or compound any proceedings thereunder.[21]) The same sweeping powers of the Malta Commissioner as derived by

16) Debates, Legislative Assembly, Sitting No. 67, Second Session, page 3491.
17) Income Tax Act, 1948, section 43 (1) (a).
18) H.A.R.J. Wilson, Income Tax and Profits Tax, page 53.
19) Sions's Income Tax, Vol. II, page 166.
20) Income Tax Act, 1948, section 73.
21) Income Tax Act, 1948, sections 74 and 75.

section 43 of the Income Tax Act are to be found in many Taxation Codes of other countries.

The position in South Africa is different in some respects and the powers of the Commissioner are still more specific and extensive. In terms of the Income Tax Act, 1941, the South African Commissioner is entitled to authorise his subordinate officers in writing or by telegram to enter any premises and search for examination, any books, records, accounts or documents. The Commissioner is also empowered to search for any moneys besides records without giving previous notice and at any time during the day. In carrying out such search, the Income Tax Officer may open or cause to be removed and opened any article in which he suspects any money, books and other documents to be contained.[22]) The Malta Commissioner is not empowered to search for monies, but inspections may be carried out during the night as well.

In the case of partnerships, the precedent partner may be required by the Commissioner to complete a separate yearly return on behalf of the partnership showing the firm's profits, the manner how the profits are allocated according to the agreement between partners and particulars of the names and addresses of the partners of the firm.[23])

Besides returns of total income from individual taxpayers and bodies of persons, the Commissioner is also empowered by the Act to request other returns containing varied information from the following:

(a) from employers—returns containing the names and places of residence of all persons employed;[24])

(b) from persons, in any capacity whatever, who may be in receipt of any profits or other income belonging to other persons or who pay to other persons any profits or income—statements containing the names and addresses of every person to whom the income belongs and other relevant information concerning such income.[25])

(c) from occupiers of any tenement, land or industrial building—returns containing the names and addresses of owners of such property, the rent payable and any other consideration passing therefor;[26])

(d) from hotel managers, lodging house owners or persons in charge of institutions—returns containing the names of lodgers or inmates[27])

When a taxpayer has delivered a return to the Office of Inland Revenue, the Commissioner may either accept it and issue an assessment accordingly or may refuse to accept the figures declared and, to the best of his judgment, may, by an order in writing, determine the amount of the chargeable income and assess him accordingly.[28]) This in departmental language, is termed "ex officio assessment" and is believed to be one of the greatest responsibilities of the Commissioner of Inland Revenue. Returns are actually examined by the Assessing Officers and to them falls the task of seeing whether to accept

22) South African Income Tax Act, 1941, section 62 (3).
23) Income Tax Act, 1948, section 49. Vide Appendix No. 11.—Form I.T. 5.
24) Income Tax Act, 1948, section 44, Forms I.T. 69 and I.T. 69A—Appendix No. 31.
25) Income Tax Act, 1948, section 46.
26) Income Tax Act, 1948, section 47.
27) Income Tax Act, 1948, section 48.
28) Income Tax Act, 1948, section 52 (2).

them or not, as will be seen in due course. In the negative, ex officio assessments and the quantum of estimated chargeable income is recommended by them. Ex Officio Assessments are raised at a figure justified by information in the possession of the Commissioner sufficient to enable the Department to go to appeal, with a reasonable hope of success.

Ex Officio Assessments may also be issued by the Commissioner (on the recommendation of the assessing officer) in the event that a taxpayer has failed to deliver a return as contemplated in the Act. A person who has been served with a notice under section 37 (1) must furnish a return even if he has no chargeable income, but an ex officio assessment would not be justified unless a proper notice has been duly served on him. An ex officio assessment will not exculpate a taxpayer from his obligation of delivering a return.[29]) Such assessment may not be revised unless the taxpayer lodges objection within fifteen days from the date of the service of the notice of assessment. For this purpose, the submission of a reasonably satisfactory return may be regarded as tantamount to the lodging of an objection.

If it is discovered that any amounts which should have been subject to tax have not been assessed to income tax, the Commissioner may cause additional assessments to income tax to be made, notwithstanding that the assessment may have become final and conclusive in terms of section 59 of the Act. The tax is charged at the rate or rates at which it would have been charged had the income not escaped assessment or full assessment as the case may be. In the United Kingdom, the position as regards additional assessments is very similar to that prevailing in Malta. The Inspector can cause additional assessments to income tax to be made, and in the case of a person who has escaped assessment altogether in any year, the Inspector of Taxes has power to make a supplementary charge, and certify it to the General Commissioners.[30])

Certain aspects of the law as regards the assessment of tax upon Limited Liability Companies are different from those prevailing in the case of ordinary businesses carried on by a sole trader or by a body of persons en nom collectif (simple partnership) section 16 of the Income Tax Act, gives wide discretionary powers to the Commissioner and in each assessment case of companies, it is up to the C.I.R. to decide whether to tax or not the undistributed profits in the hands of the shareholders. After thorough examination of the Accounts and the affairs of the Company, the Commissioner decides whether the Maltese Company could have distributed or not its profits without detriment to the maintenance and development of its business and whether the effect of such non-distribution is the avoidance of reduction of tax. In those circumstances, the Commissioner may order in writing that such undistributed profits be deemed to be distributed by way of dividends and therefore these shall be chargeable in the ordinary way in the hands of shareholders, although this dividend never reached them. The power of the Commissioner to raise tax on income which never reaches the hands of taxpayers was the cause of a heated debate in the Malta Legislative Assembly during the Committee stage of the reading of the Income Tax Bill. An Amendment to the relevant clause in the Bill carried by the House was moved by the Minister of Finance—and quoting the mover's words,

29) Income Tax Act, section 52 (3).
30) H.A.R.J. Wilson, Income Tax and Profits Tax, page 5.

the Parliamentarians ensured that "no enforcement of taxation on the part of the Commissioner of Inland Revenue on undistributed profits, which would be detrimental to the development of the trade" would ensue. As the Bill originally stood, the Commissioner of Inland Revenue had no alternative but to consider in all cases, the non-distributed profits as if they were distributed. The amendments now provide that before issuing an order in writing to charge with tax the shareholders on undistributed profits of a company, the Commissioner has to be satisfied that there has been avoidance or reduction of tax and that the company could have distributed more profits without detriment to the maintenance and development of its business.[31])

As soon as the assessment on a taxpayer or a body of persons has been worked out, a notice of assessment is served personally or sent by registered post. If any person disputes the assessment, he may apply to the Commissioner, by notice of objection in writing, to review and revise the assessment. Such objection is to be made within fifteen days from the date of the service of the notice of assessment, which period, however, may be extended by the Commissioner.[32])

The examination of an objection involves a summary process, and the exercise, on the part of the Commissioner, of judicial and quasi-judicial powers, according to the rules of natural justice.[33]) The decision of the Commissioner is given in writing. In connection with notices of objection, the Commissioner may require the person giving the notice of objection to furnish particulars and information regarding the grounds of the objection, and may summon any person to attend before him and give evidence and may examine such person on oath or otherwise, provided that the clerk, agent, servant, or other person confidentially employed in the affairs of the person to be charged and the parents, spouse or children of such person cannot be examined except on the request of the assessee.[34]) An objection may be determined either by acceptance or refusal of the Commissioner, as well as by a compromise between the Commissioner and the taxpayer who may also withdraw the objection.[35]) Any person who feels aggrieved by a decision given by the Commissioner on a notice of objection may appeal to the Board of Special Commissioners.[36])

The Malta Income Tax Act has many sections[37]) providing for the imposition by the Commissioner of penalties on persons guilty of fraudulent statements, concealment of income, making false claims, failure to keep records and make returns and other offences which are specified in the sections imposing the penalties. Some of these penalties may also be imposed by the Magistrates of Judicial Police on conviction of the defaulting taxpayer. In addition to monetary penalties, in certain cases, the Magistrates may also impose imprisonment on the offender, but the Commissioner, in his discretion, has the power to compound any offence and may before judgment stay or compound any pro-

31) Debates, Malta Legislative Assembly, Sitting No. 63, Second Session, page 3337.
32) Income Tax Act, 1948, section 55.
33) Report of the Inland Revenue Department, Malta, for the year 1955-56, page 18.
34) Income Tax Act, 1948, section 55 (3).
35) Income Tax Act, 1948, section 55 (4) and section 55 (5).
36) Income Tax Act, 1948, section 57.
37) Particularly sections 25, 63, 42/43, 72/75 of the Income Tax Act, 1948.

ceedings thereunder. No prosecution in respect of offences against the Income Tax Acet may be commenced except at the instance of or with the sanction of the Commissioner.[38])

Although it took the Parliamentarians fifteen sittings of the Malta Legislative Assembly covering a period extending over a month to debate and finally approve the second and third reading of the Income Tax Bill late in 1948, not much serious discussion developed during the passing of the aforementioned clauses relating to assessments. Few members tried to foresee the debated sections working in practice and to mould their remarks accordingly. It seems that both the government and opposition members drew red herrings and split hairs on unimporatant topics. This may be due to the feeling that developed amongst opposition members that the Government party with an overall majority in the House then, had presented Parliament with a fait accompli. It is natural that Parliamentarians are not expected to be experts in all subjects dealt with in debating proposed legislation, but they would have certainly done better if both government and opposition members criticised intelligently and constructively every clause of so important an instrument as the Income Tax Bill.

38) Income Tax Act, 1948, section 78.

U.S.A. ANTI-INFLATION ACT

On November 8, 1966 the President of the U.S.A. *signed the Investment Credit Suspension Act (PL 89-800). The period of suspension will be October 10, 1966 up to and inclusive December 31, 1967.*

This Act is an integral part of a co-ordinated anti-inflationary program. It is, together with other features of the program, designed to restrain inflationary forces by moderating economic activity in these sections of the economy where inflationary pressures are the strongest.

The reasons are explained in the report of the Committee on Ways and Means of the House of Representatives to accompany H.R. *17607, of which we give an extract.*

REASONS FOR BILL

The overall program, of which this bill is a part, is designed to moderate the pace of the economy to a level more compatible with a sustained, high level of economic growth. By removing certain tax incentives for investment in machinery, equipment, and buildings, the bill will affect those sectors of the economy where inflationary pressures are strongest. This action will also have the effect of diminishing upward pressures on interest rates and promoting an increased flow of credit into the home mortgage market. Moreover, by promoting a reduction in the demand for investment goods to a level more nearly in balance with existing capacity to supply such goods, the bill can be expected to result in a shortrun improvement in the Nation's balance of payments position.

The bill is part of a comprehensive program

This bill is a part of a comprehensive program announced by the President on September 8 to protect the uninterrupted growth of the economy at stable prices. The other elements in this program—a substantial cutback in Federal expenditures and a reduction in issues of Federal securities—will complement and strengthen the anti-inflationary impact of this bill. In combination, the various components of this program are highly interrelated and will focus anti-inflationary restraint on those sectors of the economy that require restraint.

In his message of September 8, the President stated that he would "cut all Federal expenditures to the fullest extent consistent with the well-being of our people." While determination of the precise amount of the overall reduction which will be possible cannot be made until congressional action on the remaining appropriations bills is completed, the President and the Director of the Bureau of the Budget estimate that contracts, new orders, and commitments will be reduced by at least $3 billion in the fiscal year 1967. This amount is equal to approximately 10 percent of that portion of the budget which is not allocated either to the defense effort or to payments fixed by law or

which are otherwise uncontrollable. The President has already directed that contracts, new orders, and commitments for lower priority programs be cut by $1.5 billion.

Expenditure cutbacks will be achieved in a variety of ways. In the words of the President:

> Federal civilian agencies have been directed to defer, stretch out, and otherwise reduce contracts, new orders, and commitments. Each major agency has been given a savings target, with orders to meet that target.
>
> I am prepared to defer and reduce Federal expenditures—
>
> By requesting appropriations for Federal programs at levels below those now being authorized by the Congress;
>
> By withholding appropriations provided above my budget recommendations whenever possible; and
>
> By cutting spending in other areas which have significant fiscal impact in 1967.

The third element in the administration's overall anti-inflationary program is a coordinated effort to ease the burden of monetary restrictions and promote the early reduction in interest rates. The Secretary of the Treasury has been directed to review all prospective sales of Federal securities in order to reduce to a minimum the volume of such sales in particular sectors of the money market. This effort will serve to reduce demands for long-term capital, thereby releasing more funds for private use.

The President has also called upon banks to handle money and credit equitably and to refrain from charging excessive interest. He has urged them to rely less upon high interest rates to ration available credit and more upon the use of appropriate credit ceilings.

Finally, the President has asked the Federal Reserve Board and the Nation's largest commercial banks to seize the earliest opportunity to lower interest rates. This opportunity will not arise, however, if heavy reliance must be placed on monetary policy to restrain inflationary pressures. Prompt passage of H.R. 17607, therefore, is essential to the success of this program.

The impact of this bill

The committee's bill as a part of an overall program, including the reduction of at least $3 billion in Government expenditures, will help restrain inflationary pressures by suspending for 16 months*) the investment credit for machinery and equipment and accelerated depreciation on buildings. Suspension of accelerated depreciation on buildings whose construction is begun during the suspension period complements the suspension of the investment credit. Without overlapping, the two measures combine to apply fiscal restraint over a broad sector of the market for investment goods.

By increasing the cost of items ordered, acquired, or constructed during the suspension period, the bill will reduce the potential returns from prospective investments and will discourage marginal investments. This effect will be intensified by the fact that the

*) 1 1/2 month (Act.)

investment credit will be available for machinery and equipment, ordered and acquired, or constructed after the suspension period. This effect is also intensified by the fact that accelerated depreciation will be available with respect to buildings whose construction is begun after December 31, 1967.

It is the impact on the rate of return on prospective investments rather than the revenue gain to the Government which is the most important feature of this bill from the standpoint of anti-inflationary fiscal policy. Orders for new machinery or equipment will be, and in some cases have already been, reduced relative to the large volume evident in recent months. The prompt reduction in orders will result in a decline in the size of producers' order backlogs. This will encourage producers to return to normal production schedules by reducing overtime; they will also reduce their orders for supplies and materials. These developments will lessen the pressures which have tended to produce inflationary price and wage increases in the machinery and equipment industry, commercial and industrial construction industry, and related industries.

Suspension of the investment credit increases the cost to business firms of all goods which now qualify for the credit. This increase in cost ranges from 2.4 percent in the case of machinery and equipment with an expected useful life of 4 to 6 years to 7.5 percent in the case of machinery and equipment with an expected useful life of 8 years or more. With respect to buildings, the Secretary of Commerce pointed out in his testimony before the committee that the use of accelerated depreciation methods currently provides the owners of new buildings with a benefit equivalent to at least 4 percent of the cost of the building. It is particularly worth noting that these increases in cost are temporary and can be avoided by postponing orders until after the termination of the suspension period. The bill therefore offers businessmen a strong inducement to defer investment projects until after the suspension period is terminated.

The immediate effects on economic activity which stem from a reduction in orders in capital goods are of prime importance from the point of view of restraining inflationary developments. In appraising the bill, attention should therefore be focused primarily on these effects and not on the manner in which corporate tax liabilities will be affected by the suspension. The investment credit and accelerated depreciation deductions affect tax liabilities, as a rule, only after the economic activity resulting from the production of a machine or building has been completed.

The reduction in new orders for machinery, equipment, and buildings which will result from this bill will tend to moderate the expansion in plant and equipment expenditures, and by preventing excesses will tend to forestall economic downturns in the future. Moreover, the bill is likely to have a significant impact in reducing the demand for credit by business, with the result that pressures on interest rates will be eased and more funds will become available to finance home mortgages. To the extent that the bill succeeds in preventing further increases in interest rates or in promoting a reduction in interest rates, business borrowers themselves will benefit. The reduction in interest costs to such borrowers will partially offset the effect of suspending the investment credit and accelerated depreciation with respect to buildings. By moderating the domestic demand for machinery and equipment, the bill will strengthen the balance of payments in the short run. In view of the relatively brief suspension period, over the long run the com-

petitive position of U.S. exports will continue to benefit from the availability of the investment credit.

While the bill is expected to have a significant anti-inflationary effect, it will not be of such a magnitude as to incur the risk of promoting a recession. The bill will have a marginal effect on the economy, but an effect which should direct it toward the path of full employment without price inflation.

If military requirements in southeast Asia should decrease before January 1, 1968, or if for some other reason it should become apparent that suspension of the investment credit and suspension of the use of the accelerated depreciation methods with respect to buildings are no longer necessary to restrain inflation, the Congress can promptly terminate the suspensions. The administration has also indicated that it would recommend terminating the suspension period before January 1, 1968, under such conditions.

It is not clear how the suspensions of the investment credit and accelerated depreciation will change budget receipts. There would appear to be an increase in revenue, given a level of investment. However, the suspension can be expected to reduce investment expenditures which will reduce incomes of some sellers of investment goods and thereby reduce revenues.

There is value in describing the hypothetical revenue effect of the bill, however, given the current level of investment expenditures. This, therefore, is only a description of the magnitude of the tax changes effected by this bill. The actual revenue effect will depend upon how business firms modify their investment plans in response to these suspensions.

It is estimated that suspension of the investment credit will increase receipts in the fiscal years 1967 through 1970 by $2 billion. Of this total, $350 million is expected to be received in the fiscal year 1967 and $850 million in the fiscal year 1968. The relaxation of the existing limits provided by this bill on the amounts of investment credit which may be claimed in any one taxable year will partially offset the effect of suspending the credit as far as the fiscal years 1968 through 1970 are concerned. This provision will reduce tax receipts in those 3 fiscal years by $850 million. In the fiscal year 1968, the relaxation in the limitation will reduce receipts by $125 million, reducing the net effect of the investment credit provisions to an increase in receipts in that year of $725 million. Suspension of accelerated depreciation with respect to buildings and structures constructed during the suspension period will increase receipts during the fiscal years 1968 through 1970 by an estimated $125 million. The effect in the fiscal year 1968 will be an increase of $15 million.

DEVELOPMENTS IN INTERNATIONAL TAX LAW

As was stated in the December 1966 issue the Standing Committee of Heads of the Revenue Department of the E.E.C. agreed that a multilateral convention would be a suitable means, on the whole, of regulating the avoidance of double taxation in the E.E.C. Such a multilateral convention would be a complex question; not least because each tax system has a long history based upon traditional developments in each country. In Africa such a long history does not exist. In the French speaking countries tax systems are all based on the same (old) French patterns. Mutual consultations would not be handicapped by the developments in the European way. During a session in 1963 at Abidjan (Ivory Coast) a *Project to an African multilateral tax convention* has been developed between the members of the O.A.M.C.E. (Organisation Africaine et Malgache de Coopération Economique).

The text of this project is the subject of the Supplement to this Bulletin issue. Along the lines of this text France has concluded a number of bilateral tax conventions with African states, as is stated in the Supplement. It is to be expected that the treaties which are under negotiation will also be strongly influenced by the project of the African multilateral convention which, however, has not yet been signed by the African countries.

On the 9th of September 1966 France concluded a new treaty with Switzerland. The treaty history has already been described on p. 508 of the 1966 issues of the Bulletin. The instrument of ratification has not yet been exchanged, but after ratification the treaty will be effective as of January 1, 1967. The treaty is not only of specific significance to the French-Swiss tax relationship, but, being the first treaty after the French tax reform, may be an example for future French treaties. The treaty is also directed against tax avoidance; the French administration thought the Swiss national rules of December 1962 too liberal*).

The text, together with the *Swiss* and *French* motives of the new convention will be the subjects of a coming edition in the series "Publications of the International Bureau of Fiscal Documentation"; a more elaborate discussion will appear in a future issue of "European Taxation".

The new *Swiss-Dutch* tax treaty, concluded June 22, 1966 is also directed against tax avoidance, but in quite another way from the new French-Swiss treaty. It abolishes a large number of the advantages of Switzerland as a tax haven for Dutch taxpayers. Explanation will be given by a Dutch and Swiss expert in another coming edition in the series "Publications of the International Bureau of Fiscal Documentation". After the new Swiss-Swedish convention**) new conventions explicitly limiting the possibilities of tax avoidance have been added to the list of bilateral tax treaties. The purpose of modern tax treaties is more than the simple avoidance of double taxation!

*) Compare: Swiss measures against abuse of tax conventions by Dr. Kurt Locher and Dr. Walter Ryser; Publications of the International Bureau for Fiscal Documentation, no. 19 (1963).

**) Published in the Bulletin 1965, p. 367.

* * * * BIBLIOGRAPHY * * * *

AUSTRALIA

WHAT IS INCOME? (Definition, History of Income Tax; Capital Gains) by *Justice Bright* of the Supreme Court of South Australia with commentaries thereon by *M.D. Oakeshott* and *S.J. Jacobs*.

Paper presented at the Taxation Convention arranged by The South Australian Division of the Taxation Institute of Australia 6-8 May 1966; 29 Bligh Street, Sydney. 14 pp.

The question, what is income, is a question which proved to be timeless and world-wide. The last words of Mr. Jacobs' commentary may not be too far from the truth in quoting from a speech of Lord Atkin in the House of Lords:

"I know of only one authority which might justify the suggested method of construction: "When I use a word", Humpty Dumpty said in a rather scornful tone, "it means just what I choose it to mean, neither more nor less". "The question is", said Alice, "whether you can make words mean so many different things". "The question is", said Humpty Dumpty, "which is to be master? —that's all".

Library International Bureau of Fiscal Documentation, Australia Broch. no. 73.

CANADA

Queens University is publishing a series of Papers in Taxation and Public Finance. No. 3, 161 pp., which appeared in October 1966 contained a paper including the following subjects:

ALTERING THE TAX STRUCTURE TO PROMOTE ECONOMIC GROWTH by *Douglas C. Brown;*

THE FISCAL PERFORMANCE OF INDIRECT TAXATION by *Kenyon E. Poole;*

SOME ASPECTS OF A VALUE-ADDED TAX FOR CANADA by *Richard Malt;*

LE JEU ETATISE AU QUIBEC? by *J.A.H. Cannone;*

REVENUES PRODUCTIVITY OF THE REAL PROPERTY TAX (Ontario) by *Frank A. Clayton*

The increased concern over questions of equity and stable economic growth as well as the intensive and extensive expansions in governmental functions has led to re-evaluation of tax-structure. In Canada this may be observed in the numerous Royal Commissions and special committees which have been established in recent years for the purpose of investigating the federal and provincial revenue systems. The purpose of this collection of articles is to expose the reader to a variety of Canadian tax-problem areas and to an evaluation of some of the possible solutions.

Library International Bureau of Fiscal Documentation, no. 42 B 38; 1678-1966.

DEVELOPING COUNTRIES

PUBLIC FINANCE AS AN INSTRUMENT FOR DEVELOPMENT, papers prepared for a study course held under the auspices of the Technical Co-operation Programme of the O.E.C.D. published in the series "Problems of Development", edited by Alan T. Peacock; publisher Organisation for Economic Co-operation and Development, Paris, 1965, 112 pp.

In this paper:

Alan T. Peacock: INTRODUCTION—FISCAL POLICY FOR ECONOMIC DEVELOPMENT IN THEORY AND PRACTICE;

Andreas Michalakis: FISCAL POLICY AND ECONOMIC DEVELOPMENT IN GREECE;

V. Xavier Pintado: THE FISCAL SYSTEM AND ECONOMIC DEVELOPMENT IN PORTUGAL;

Thomas Galan: THE PLACE OF THE FISCAL SYSTEM IN THE SPANISH ECONOMY;

Gerard Hauser: FISCAL SURVEY OF TURKEY.

Library International Bureau of Fiscal Documentation, no. 1664-1966.

PROBLEMS OF ECONOMIC GROWTH AND PLANNING: THE SUDAN EXAMPLE by *Rolf Güsten;*

Springer Verlag Berlin 1966, published in the series "Schriftenreihe Afrika-Studien" No. 9, IFO – Institut für Wirtschaftsforschung, 1966, 61 pp., price DM 13,50.

Although this study is concerned with some problems of growth of a particular country, the Republic of the Sudan, its real subject is method. How can we, so runs the question, acquire standards by which to judge a development plan; how

can we demarcate growth possibilities in an economy.

Library International Bureau of Fiscal Documentation, No. 42 B 33; 1658-1966.

"United Nations", New York, has published a number of studies on development, We have recently received: DEVELOPMENT PLANS: APPRAISAL OF TARGETS AND PROGRESS IN DEVELOPING COUNTRIES (World Economic Survey 1964—Part 1), 1965;
THE FINANCING OF ECONOMIC DEVELOPMENT (World Economic Survey, Part 1), 1966;
AFRICAN AGRICULTURAL DEVELOPMENT, Food and Agricultural Organization of the U.N., 1966;
SITUATION, TRENDS AND PROSPECTS OF ELECTRICA POWER SUPPLY IN AFRICA.
United Nations publications may be obtained from bookstores or U.N., Sales Section, New York or Geneva.

GERMANY

C.H. Beck's Verlagsbuchhandlung, Munich and Berlin, has published an excellent book on German taxes on foreign relations:
DEUTSCHE STEUERN BEI AUSLANDSBEZIEHUNGEN. The authors are *Dr. Albert J. Rädler* and *Arndt Raupach*. Price DM 78,—., XXXI, 678 pp.

The 35 chapters deal with the following subjects in so fas as they relate to the aspects of importance to foreign relations:
Beförderungsteuer, Börsenumsatzsteuer, Einkommensteuer, Erbschafsteuer, Gesellschaftsteuer, Gewerbesteuer, Grunderwerbsteuer, Körperschaftsteuer, Kraftfahrzeugsteuer, Umsatzsteuer, Umsatzausgleichsteuer, Verbrauchsteuer, Vermögensteuer, Wechselsteuer, Entwicklungshilfesteuergesetz, E.W.G. Vertrag, GATT and the taxation of international concerns.
The authors have tried to make clear that international tax law is not isolated but a part of the legal order; viewpoints of constitutional law, international public law and administrative law are evaluated. Attention has been paid to the EEC tax problems—especially in the field of turnover taxation. This book is of particular value to the practitioner as it provides comprehensive coverage of all relevant problems including full reference to case law, rules and literature.

Library International Bureau of Fiscal Documentation, no. 41 E 10: 1680-1966.

The 1965 German tax bibliography (Band XIII): FUNDHEFT FÜR STEUERRECHT has been published. It contains about 11,150 tax publications, case law and administrative regulations. The bibliography is organized on the bases of an article per article referring to the respective tax laws.
An equally extensive index covering preceding volumes from the years 1960-1965 is enclosed.
Attention has been paid to literature on foreign tax law.
The bibliography has been published by C.H. Beck's Verlagsbuchhandlung, Munich and has been compilated by *H. Ziemer, H. Kalbhenn, Dr. G. Felix* with the co-operation of D. Carlé, Dr. Hänecke, Dr. Huiskamp, Dr. Karametz and Dr. Klimowsky. 619 pp., DM 72,50.

Library International Bureau of Fiscal Documentation, 25 V 499; 1727-1966.

U.S.A.

CCH STATE TAX HANDBOOK as of September 15, 1966, published by Commerce Clearing House Inc., Chicago.
Here you will find a brief description of the state wide levies, including the District of Columbia, the basis and rates of each tax and the principal payment and return due dates. The material in this handbook is reproduced from CCH State Tax Guide.

Library International Bureau of Fiscal Documentation, no. 42 B 35; 1665-1966.

PROCEEDINGS OF THE THIRTY-SEVENTH AND THIRTY-EIGHTH ANNUAL MEETINGS OF THE NATIONAL TOBACCO TAX ASSOCIATION 1963-1964. Dellas, Texas, October 1963, published by the Federation of Tax Administrators, 1313 East Sixtiest Street, Chicago. 87 pp.
From the contents:
REPORT OF THE COMMITTEE ON TAX EVASION; THE CIGARETTE TAX—THEN AND NOW by *Sam Kimbertin;*
A UNIFORM STATE TAX PROCEDURE CODE by *Lawton L. Livinger;*
EDP (ELECTRONIC DATA PROCESSING) AND THE TAX ADMINISTRATION by *John K. Coleman;*
RECENT DEVELOPMENTS IN FEDERAL TOBACCO TAX ADMINISTRATION by *Charles J. Mouhtouris.*

Library International Bureau of Fiscal Documentation, U.S.A. Broch. no. 228.

CCH has published INVESTMENT CREDIT AND ACCELERATED DEPRECIATION SUSPENDED LAW AND EXPLANATION. (PL 89-800). Signed by the President. November 8, 1966, 64 pp.

The reasons for this anti-inflation act are described on p. 39 of this Bulletin.

The suspension deals with machinery and equipment which a businessman purchases or starts to contract during the period October 10, 1966 through December 31, 1967. He will not get an investment credit on this equipment even though he waits until after 1967 before putting it into service. There are a number of exceptions, of course covering situations where orders, contracts, or plans are binding or over half completed before October 10. All this is explained in this CCH report.

Library International Bureau of Fiscal Documentation, U.S.A. Broch. no. 227.

INCOME TAX REGULATIONS: "fixed" and "proposed" under Internal Revenue Code: Volume one and Volume two, publication of Commerce Clearing House Inc. (CCH), Chicago.

Ranking in importance directly under the Internal Revenue Code are the Regulations issued by the Treasury Department. These official Regulations comprise a separate series: this series is compiled with the texts of all proposed Regulations or proposed amendments to the final Regulations in these two volumes. A complete index to all the Regulations is also included.

Library International Bureau of Fiscal Documentation, no. 42 C 34 and 35; 1610 and 1611-1966.

MACRO ECONOMICS, FISCAL POLICY, AND ECONOMIC GROWTH by *Norman F. Keizer*, Associate Professor of Economics, San Jose State College; John Wiley & Sons Inc., New York, London, Sydney; 1966, 525 pp., price 113/— sh.

An attempt has been made to bring together the wide variety of theory, ideas and materials necessary for an understanding of fiscal policy. Basically the authors have been attempted to:

1) review the macro economic theory necessary to an understanding of fiscal policy;
2) apply this theory to the area of fiscal policy;
3) discuss the problems involved in the procedures, conflicts and special techniques of fiscal policy; and
4) evaluate and suggest improvements in fiscal (and monetary) policy. Monetary theory and monetary policy are areas to which a part of the book is devoted.

Library International Bureau of Fiscal Documentation, no. 41 A 21; 1622-1966.

AMERICAN FEDERAL TAX REPORTS, Second Series, Vol. 17, Prentice Hall Inc., Englewood Cliffs N.J., 1966, 1547 pp.

This volume contains unabridged federal and state court decisions arising under the federal tax laws. The cases were first printed as Advance Sheets and sent to subscribers during the first half year of 1966. Advance sheets of each case are submitted to the president judge; so he can make corrections and changes before it is reproduced in the bound volumes. Two bound volumes are issued each year.

Library International Bureau of Fiscal Documentation, no. 14 A 19; 1621-1966.

2. LOOSE-LEAF SERVICES

Releases between October 1 and November 30, 1966

AUSTRIA

Die Einkommensteuer, release 4.
Wirtschaftsverlag Dr. Anton Orac, Vienna.
Österreichische Steuer- und Wirtschaftskartei, releases 19-22. Industrieverlag Peter Linde, Vienna.

BELGIUM

Documentatie Vandewinckele – De Nieuwe Inkomstenbelasting, releases 284-290.E.K. Vandewincke-le, Brugge.
Guide fiscal permanent, release 275. Gaston van den Avyle, Brussels.
Handleiding der Inkomstenbelasting, releases 13-14. Samson N.V., Brussels.
Traité des Taxes assimilées au Timbre, release 38. Joseph Otten, Directeur de l'Enregistrement et des Domaines à Liège.

CANADA

Canadian Income Tax – f.G. Mc Donald, release 33. Butterworth and Co., Canada Ltd., Toronto.

Canada Tax Service Letter, release 97. Richard de Boo Ltd., Toronto.

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Mc Donald's current Taxation, release 36-44. Butterworth & Co., Toronto.

Provincial Taxation Service, release 207 and 208. Richard de Boo Ltd., Ontario.

DENMARK

Skattebestemmelser i systematisk fremstilling, release 24 and 25. A.S. Skattekartoteket Informationskontor, Copenhagen.

FRANCE

Bulletin de Documentation pratique des Impôts directs et des droits d'Enregistrement, release 7. Editions Francis Lefebvre, Paris.

Code annoté des Contributions directes, release 37. Ed. Sétéca, Paris.

Dictionnaire Fiscale Permanent, releases 28-32. Editions Législatives et Administratives, Paris.

Documentation pratique de Sécurité sociale et de Législation du Travail, releases 10-11. Francis Lefebvre, Paris.

Droit des affaires, releases 9-10. Editions législatives et Administratives, Paris.

Droit des Affaires dans les pays du Marché Commun, release 38. Ed. Jupiter, Paris.

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1) *Chiffre d'affaires, a) Code fiscal,* release 5144;
2) *Impôts directs, a) Commentaire "Impôts Directs",* release 1067;
b) *Code fiscal "Impôts directs",* release 145. Ed. Techniques, Paris.

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GERMANY

ABC Führer Lohnsteuer/Hartz-Over, release 57. Fachverlag für Wirtschafts- und Steuerrecht, Schäffer und Co., Stuttgart.

AO Kommentar-Hübschmann-Hepp-Spitaler, release 47-48. Dr. O. Schmidt KG, Cologne.

Einkommensteuer-Körperschaftsteuer, release 5. Verlag C.H. Beck, Munich.

Deutsche Gesetze/Schönfelder, release: Oct. 1966. Verlag C.H. Beck, Munich.

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Kommentar Bewertungsgesetz-Vermögensteuergesetz, release 22. Verlag Dr. Otto Schmidt, Cologne.

Kommentar zur Einkommensteuer einschl. Lohnsteuer und Körperschaftsteuer, release 70. Verlag Dr. Otto Schmidt, Cologne.

Reichsabgabenordnung, release 4. Verlag Dr. Otto Schmidt, Cologne.

Schnellkartei des deutschen Rechts, release 135. Verlag Dr. Otto Schmidt K.G., Cologne.

Steuererlasse in Karteiform, releases 61-62. Dr. Otto Schmidt K.G., Cologne.

Steuergesetze, releases Sept. C.H. Beck's Verlagbuchhandlung, Munich.

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NETHERLANDS

Beknopte Belastinggids – Smeets en Meihuizen, release 38. L.J. Veen's Uitgevers Mij. N.V., Amsterdam.

Belastingberichten, releases 60-63. N. Samson N.V., Alphen a/d Rijn.

Belastingwetgevingserie:
Zegelwet, release 10;
Loonbelasting, release 4;
Inkomstenbelasting, release 7;
Wet op de vermogenbelasting, release 2.
F. Noorduyn en Zn. N.V., Gorinchem.

Belastingwetten, release 8. N.V. Uitgeversmaatschappij S. Gouda Quint – D. Brouwer en Zoon, het huis de Crabbé, Arnhem.

FED losbladig fiscaal Weekblad, release 1064-1072. N.V. Uitgeverij FED, Amsterdam.

FED's fiscaal Repertorium, release 5-6. N.V. Uitgeverij FED, Amsterdam.

Handboek voor de Europese Gemeenschappen: 13 *Verdragteksten en aanverwante stukken,* releases 24-25-26. N.V. Uitg. Mij. AE.E. Kluwer, Deventer.

Tariefijsten voor de EEG, release 55. N.V. Uitg. Mij. AE.E. Kluwer, Deventer.

Handboek voor in- en uitvoer:
a) *Belastingheffing bij Invoer,* releases 67-68;
b1) *Tarief van Invoerrechten,* releases 79-80;
b2) releases 48-49.
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Kluwer's fiscaal Zakboek, release 10. N.V. Uitg. Mij. AE.E. Kluwer, Deventer

Nederlandse Belastingwetten – de Groot, release no. 25-26 N. Samson N.V., Alphen a/d Rijn.

Nederlandse Regelingen van internationaal Belastingrecht, suppl. 3 and 4. N.V. Uitg. Mij. AE.E. Kluwer, Deventer.

Leidraad bij de Belastingstudie, release 7. S. Gouda Quint – D. Brouwer en Zoon, Arnhem.

Regelingen Euromarkt, releases 71 and 72. Vermande en Zonen, IJmuiden.
Teruggaaf van Omzetbelasting bij Uitvoer, release 176 and 177. N. Samson N.V., Alphen a/d Rijn.
Vademecum voor In- en Uitvoer, releases 344-348. N.V. Uitg. Mij. AE.E. Kluwer, Deventer
De Vakstudie – Fiscale Encyclopedie:
Vennootschapsbelasting, release 58;
Successiewet, releases 18, 19 and 19A.
Wet op de Inkomstenbelasting, releases 23 and 24. N.V. Uitg. Mij. AE.E. Kluwer, Deventer.
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Tabakswet, release 2;
Invorderingsrecht van de fiscus, release 2.
N.V. Uitg. Mij. AE.E. Kluwer, Deventer.
Vennootschappen, Verenigingen en Stichtingen.
Deel A: release 15 and 16;
Deel B: release 12
N.V. Uitg. Mij. AE.E. Kluwer, Deventer.

NORWAY
Skatte-nytt A, release 11. Norsk Skatte betalerforening, Oslo.

SPAIN
Circulares - boletines de informacion, releases 88-90. Gabinete de Estudios (T.A.L.E.) Madrid.

SWITZERLAND
Die Steuern der Schweiz, releases 32, 34 and 36. Verlag für Recht und Gesellschaft A.G., Basel

SYRIA
Code fiscal syrien permanent, release 31. Damascus.

TURKEY
Türk Argüs Ajanski - La Législation Turque, releases 3479-3525. Karaköy Istanbul.

UNITED KINGDOM
British Tax Encyclopedia, Vol. II, release 18. Vol. III, release 18. Vol. V, release 18. Sweet and Maxwell Ltd., London E.C.4.
Income Taxes outside the Commonwealth, release 10. Her Majesty's Stationery Office, London.

U.S.A.
Federal Tax Guide Reports, releases 1-7.
Commerce Clearing House, Chicago.
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Prentice Hall Inc., Englewood Cliffs, New Jersey.
Tax Treaties, release 176. CCH Chicago.
State Tax Guide, releases 360-363. CCH, Chicago.

Continued on the following pages with other important announcements

Aktuell und wichtig für alle Steuerpflichtigen,
die Auslandsbeziehungen unterhalten

Rädler-Raupach

Deutsche Steuern bei Auslandsbeziehungen

von Dr. Albert Joseph Rädler und Arndt Raupach
1966. XXXI, 678 Seiten gr. 8°. In Leinen DM 78.—

Wer mit der Praxis internationaler Steuerfälle vertraut ist, weiß, wie sehr deren Lösung meist von einer Vielzahl sich teilweise überschneidender Gesichtspunkte abhängt. Abgesehen von den verschiedenen Steuerarten kommt dabei auch den Fragen des formellen Steuerrechts eine gewichtige Rolle zu. Aus diesem praktischen Bedürfnis heraus ist diese Schrift zweier Fachleute – eines Betriebswirtes und eines Juristen – entstanden. In 35 Kapiteln werden folgende Gebiete behandelt, soweit sie bei Auslandsbeziehungen Bedeutung erlangen:

Beförderungsteuer, Börsenumsatzsteuer, Einkommensteuer, Erbschaftsteuer, Gesellschaftsteuer, Gewerbesteuer, Grunderwerbsteuer, Körperschaftsteuer, Kraftfahrzeugsteuer, Umsatzsteuer, Umsatzausgleichsteuer, Verbrauchsteuern, Vermögensteuer, Wechselsteuer; ferner Entwicklungshilfesteuergesetz, EWG-Vertrag und GATT sowie die Besteuerung internationaler Konzerne.

Der Praktiker wird es vor allem begrüßen, daß hier die Auslandsfragen, die in den Kommentaren zu den einzelnen Steuergesetzen verstreut und meist nur am Rande behandelt sind, eine ausführliche und zusammenfassende Darstellung gefunden haben. Dabei sind Rechtsprechung und Literatur vollständig verarbeitet und zahlreiche Beispiele und tabellarische Übersichten beigefügt. Das Buch ist daher besonders geeignet für inländische Unternehmen, die sich im Export betätigen oder Niederlassungen im Ausland unterhalten, für ausländische Unternehmungen mit Geschäftstätigkeit oder Niederlassungen in Deutschland, für Wirtschaftsverbände, Banken und Versicherungen, rechts- und steuerberatende Berufe und Notare.

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Internationale Wirtschafts-Briefe (IWB)

Neben dem Aussensteuerrecht und dem Aussenwirtschaftsrecht der Bundesrepublik Deutschland wird in den IWB das Recht aller Staaten des Erdballs behandelt. Besondere Berücksichtigung finden die immer wichtiger werdenden EWG-Fragen. Die Zeitschrift INTERNATIONALE WIRTSCHAFTS-BRIEFE vereinigt in sich die Vorzüge eines aktuellen Informationsdienstes mit einem Sammelwerk in Loseblattform, das nach Ländern und Sachgebieten gegliedert ist. Das Sammelwerk enthält u.a. sämtliche deutschen Doppelbesteuerungsabkommen.

Die Zeitschrift INTERNATIONALE WIRTSCHAFTS-BRIEFE erscheint zweimal monatlich. Mühelos läßt sie sich im Sammelwerk ablegen und hält es immer auf dem neuesten Stand. Der Bezugspreis für die Zeitschrift beträgt monatlich DM 7,50, für Angehörige der IFA DM 7,— und für in Ausbildung befindliche Personen DM 6,—. Das Sammelwerk hat mit Stand vom 1.1. 1967 einen Umfang von rd. 5.500 Seiten. Einschließlich 6 Spezialordner und ausführlichen Stichwort- und Inhaltsverzeichnissen kostet dieses umfassende Nachschlagwerk DM 110,—

Klage- und Prozessrecht des EWG-Vertrages mit Entscheidungssammlung

von Rechtsanwalt Dr. Dietrich Ehle/1966, Loseblattwerk, 1064 Seiten einschl. 1. Ergänzung, Stand Dezember 1966, 2 Balacron-Ordner, Verlags-Nr. 6007, DM 183,—.

Die Bedeutung des Gemeinschaftsrechts für die praktische Rechtsanwendung und eine schon jetzt umfangreiche Rechtsprechung des Gerichtshofes zum EWG-Recht machen einen systematischen Kommentar zum Klage- und Probeßrecht des EWG-Vertrages notwendig.

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Verlag Neue Wirtschafts-Briefe
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- ☐ Excise taxes
- ☐ Federal taxes
- ☐ Franchise taxes
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92 2. *Loose-leaf services:* Algeria, Austria, Belgium, Canada, Denmark,
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I.F.A.

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COMPETITION
FOR THE MITCHELL B. CARROLL PRIZE

The INTERNATIONAL FISCAL ASSOCIATION with headquarters c/o Building Amsterdam-Rotterdam Bank N.V., 43 Rokin, Amsterdam-C., Netherlands, and composed of members in 68 countries, has instituted in recognition of the work of its president in the field of fiscal law, a prize which has been named the "Mitchell B. Carroll Prize".

The detailed conditions governing the award of the prize are given below.

1 The prize shall be awarded for a typewritten or printed paper devoted to international taxation or comparative law. In even years (1968, 1970) it will be awarded for a work of legal nature and in odd years (1967, 1969) for one of an economic character.

2 All persons under 35 years of age on the 31st July of the year in question may compete whether they are members of the Association or not.

3 The paper must not have been printed more than 2 years previously, and if it is a thesis for a doctor's degree, the defence of it must not have taken place more than 2 years previously, this period being counted from the 1st of January of the year of printing or defence of thesis.

4 Papers may be entered by the authors themselves, but the national branches of I.F.A. or even individual members, domiciled in countries where a national branch is lacking, may submit papers not directly submitted by the authors of them.

5 The Jury shall only accept original work making either a theoretical or a practical contribution to the study of the effects of taxation, whether it concerns international taxation or comparative tax law.

6 Only papers written in one of the three official languages of I.F.A. (English, French and German) will be accepted for the competition.

7 The Jury is made up in such a way that its decisions are based on some continuity of opinion:
— 3 members are appointed for six years: one jurist, one economist and one professional man (e.g. barrister, civil servant). These members can be reappointed on expiry of their term;
— 2 members appointed each year, for one competition only, jurists for even years and economists for odd years.

8 There is no restriction on the number of pages of the paper. No precise subject is laid down for the candidates.

9 The winner shall receive a medal and an invitation to attend the congress during which the prize is awarded. Upon application by him, a contribution not exceeding U.S.$ 200,— shall be granted towards the expenses, entailed by his attendance at the congress.

10 The Jury's decision shall be made known at least two months before the prize is awarded in order to make it possible for the winner to attend the congress.

11 Papers entered for the prize for a given year must be submitted to the Jury in sevenfold before or on the 1st of May of the year in question.

12 Address of the Jury: General Secretariat of I.F.A., c/o Amsterdam-Rotterdam Bank N.V., 43 Rokin, Amsterdam-C., Netherlands. President of the Jury is Professor Jean Baugniet, Pro-Recteur de l'Université Libre de Bruxelles, Belgium.

* * * * ARTICLES * * * *

ROBERT B. HODES*, ARTHUR A. FEDER*

AN INTRODUCTION TO DOING BUSINESS IN THE UNITED STATES UNDER THE FOREIGN INVESTORS TAX ACT OF 1966

I. INTRODUCTION

The Foreign Investors Tax Act of 1966[1]) embodies the most extensive revision of the tax laws affecting foreign persons investing or doing business in the United States ever accomplished.[2]) The Act is a key element of a general revision of the tax laws relating to foreign investment in the United States and American investment abroad that has taken place since 1962.[3]) The income tax provisions of the Foreign Investors Tax Act

*) Members of the New York Bar. The authors wish to express their gratitude to their associate, Sherwin S. Zeitlin of the New York Bar, without whose help this paper could not have been written.

1) Public Law 89-809, 80 Stat. 1539 (1966). The Act originally was recommended by President Johnson on February 10, 1965. H.R. 5916 was submitted to Congress by the Treasury Department on March 8, 1965. After Hearings, the House of Representatives Ways and Means Committee instructed its Chairman Mills to introduce H.R. 11297, a modified version of H.R. 5916. On February 28, 1966 Chairman Mills introduced a further revised bill, H.R. 13103. H.R. 13103 was reported by the House Ways and Means Committee on April 26, 1966, and passed the House without opposition. H.R. 13103 was reported with amendments by the Senate Finance Committee, and was passed by the Senate with additional amendments on October 13, 1966. A Conference version of the bill was passed by both Houses on October 22, 1966 and signed by the President on November 13, 1966.

2) The 1966 Act is the first broad revision of the tax laws governing foreign taxpayers since the Revenue Act of 1936. 49 Stat. 1648 (1936).

3) In 1962 the Internal Revenue Code was amended to increase the tax burden on American enterprise conducted abroad. Public Law 87-834, 76 Stat. 960 (1962). A large number of tax conventions have been negotiated, and the process of negotiating new ones and revising old ones goes on. For example, in the last four years the conventions with Germany, The Netherlands and the United Kingdom have been extensively revised. New treaties with Israel, Luxemburg, the Phillipines, and Thailand have been negotiated. See discussion in Surrey, The United States Tax System and International Relationships—Current Developments, 1965-6(1), Bulletin for International Fiscal Documentation 45 (1966). In 1966 the Treasury Department proposed and is now about to adopt regulations dealing with allocation of income and expenses between United States and related Foreign

After Mr. Leo S. Ullman's analysis of the estate and gift tax provisions of the Foreign Investors' Tax Act, 1966 which was published in the January 1967 issue, we now publish a comprehensive survey of the income tax provisions of the same Act. The impact of the changes on foreign investment in the United States is considerable. For further details, readers are referred to the 800-page loose-leaf service "United States Income Taxation of Foreign Corporations and Nonresident Aliens" by Sidney I. Roberts and William C. Warren and the first 400-page supplement thereto, both recently published by Practising Law Institute and the International Bureau of Fiscal Documentation. *Editor's Note*

(hereinafter called the "Act" or the "FITA"), which are generally effective for a taxpayer's first taxable year beginning after December 31, 1966,[4]) reflect changes of profound importance to foreigners having either investments within the United States, or business operations with significant contacts in the United States. The Act will also affect foreign corporations controlled by the United States interests whose tax position was unaffected by the foreign corporation provisions of the Revenue Act of 1962.[5]) In some cases the Act will for the first time reach beyond the shores of the United States to tax income that formerly was not subject to United States taxation.

The genesis of the Act was the Report of the Fowler Task Force of 1964,[6]) which made a variety of recommendations for changes in the income, estate and gift tax laws, aimed at eliminating obstacles to foreign investment in the United States, thus improving the balance of payments. In its final form the Act adopts some, but not all, of those recommendations. It also attempts to serve other ends, such as the modernization of the Code and the prevention of the use of the United States as a tax haven,[7]) which are unrelated to the original aims of the Fowler Task Force. Consequently, the statute as finally enacted may, paradoxically, in some cases operate to adversely affect the United States balance of payments.

This paper will focus on commercial activities carried on in the United States by foreign corporations.[8]) The continued application of the United States estate tax to the United States assets of foreign individuals will lead in most cases to the use of a corporation, and in all likelihood a foreign corporation, as the vehicle for carrying on such an enterprise. Our discussion of investment activities will concentrate on those related to contemporaneous business operations of the same enterprise.

We will try to give a practical view of the chief points of the act, with some reference to questions of interpretation for which only tentative conclusions are possible at this stage.

The reader should bear in mind that under United States procedures the passage of a new statute is only the first step in a long process of official interpretation. Some time in 1967 or 1968 the Treasury will propose and (after hearings) adopt what one must

Taxpayers. Proposed Regulations §§ 1.482-1 and 1.482-2, 667CCH Par. 8801 (1966). These regulations will have a large bearing on the tax burdens imposed upon the international transactions of United States business. There has also been a sharp increase in enforcement activities in this area.

4) Foreign Investors Tax Act of 1966 §§ 102(e), 103(n), 104(n), 105(d). Thus, a corporation using an October 1—September 30 taxable year would not be subject to the effects of the FITA until October 1, 1967.

5) I.R.C. § 951 et seq.

6) Report to the President of the United States From the Task Force on Promoting Increased Foreign Investment in United States Corporate Securities and Increased Foreign Financing for United States Corporations Operating Abroad (1964).

7) H.R. Rep. No. 1450, 89th Cong. 2d Sess. 6 (1966); S. Rep. No. 1707, 89th Cong. 2d Sess. 9 (1966). Hereinafter cited as H.R. Rep. or S. Rep.

8) With one exception (not here relevant) stock and debt obligations of a domestic corporation are subject to estate taxation at the death of a foreign individual, who dies owning them. Unless held by a former American citizen who expatriated himself after March 8, 1965, stock and debt obligations of a foreign corporation are free of the estate tax, even if that corporation carries out all of its activities in the United States. I.R.C. §§ 2104, 2107.

expect to be a complex set of regulations setting forth the initial administrative view of the Act.

The Internal Revenue Service ordinarily will decline to rule on most questions of interpretation until those final regulations have been issued. Until then, much reliance will have to be placed upon the Committee Reports which embody the legislative history of the Act, and which in this case reflect a conscientious effort to clarify as far as possible doubtful matters which were called to the attention of the Treasury and Congress while the Act was under consideration. In view of this prospect, this paper must be considered to be an introduction to the Act.

The conclusions set forth herein are primarily those dictated by the domestic law of the United States. They may be modified by applicable income tax conventions.[9]) We have tried to indicate the effects of typical treaty provisions upon the results specified by the Code. However, in view of the variety of treaty provisions and the complexity of the subject, this aspect of our paper is admittedly less than complete.

II. PRE-1966 LAW AND GENERAL EFFECTS OF THE FITA

A. *Prior Law*

Under prior law foreign corporations were divided into two groups—those engaged in trade or business in the United States at any time during the taxable year ("ETB"), and those not so engaged.[10]) A foreign corporation engaged in trade or business in the United States was taxable at U.S. income tax rates applicable to domestic taxpayers with respect to *all* income and gains from sources within the United States, whether or not that income had any connection with the business carried on in the United States. Deductions were allowed to the extent that they were connected with the income from sources within the United States, but only if a "true and accurate" return was filed.[11]) The Code, therefore, incorporated the "force of attraction" principle which had also appeared in the earlier United States Income Tax Conventions.[12]) Thus, if a foreign corporation operated a factory in the United States, income from manufacturing operations carried on in the factory was taxable in the United States. Because the taxpayer

9) The provisions of income tax conventions are paramount over any change made by the FITA. FITA § 110.

10) The ETB concept serves somewhat the same function as the concept of "permanent establishment" under the older U.S. income tax treaties. Under those treaties, a foreign taxpayer generally lost all of the advantages otherwise accorded under the treaties, if he maintained a permanent establishment in the United States. See, for example, U.S.-Australia Income Tax Convention, Article III; U.S.-Canada Income Tax Convention, Article I; U.S.-France Income Tax Convention Article 3. A foreign taxpayer who did not have a permanent establishment was not subject to U.S. taxation on any industrial and commercial profits realized, even though from U.S. sources, and was generally accorded other benefits such as reduced rates of withholding tax on interest and dividends.

11) I.R.C. (pre-FITA) § 882(c)(1), (2). Throughout this article this form of citation is used to refer to the Internal Revenue Code of 1954, as amended, immediately before the effective date of the FITA. References to the Code as amended by the FITA will be given as I.R.C.

12) See note 10, supra.

was engaged in trade or business in the United States, interest on bonds of publicly owned American corporations held as investments would be taxable at the full 48 percent U.S. corporate tax rate, rather than at the flat 30 percent rate which would have been collected if the corporation had not been in business in the United States. Similarly, capital gains realized on sales of investment securities in the United States were taxable at capital gain rates in the case of a corporation engaged in trade or business in the United States.[13])

On the other hand, corporations which were not engaged in trade or business were taxed at the flat rate of 30 percent on gross income from sources within the United States that constituted "fixed or determinable annual or periodical" income. This included interest, dividends, rents, salaries, wages, premiums, compensations, remunerations and emoluments and other types of "fixed determinable annual and periodical" income, such as royalties.[14]) All other income, such as income from sales of property, even though having its source in the United States, was free of taxation, since it was not fixed, determinable, annual or periodical income.

Whether or not engaged in trade or business in the United States, foreign taxpayers were taxed only upon income from United States sources.[15]) Thus, if a corporation engaged in trade in the United States sold United States securities but transferred title to the vendee in a foreign country, the gain would not be taxable in the United States.[16]) Similarly, if a United States office of a foreign taxpayer negotiated a sale of goods from Germany to Mexico, with title passing in either of the foreign countries, no United States source income arose from the transaction, and no U.S. tax was payable.[17]) Or, if the U.S. office of a foreign corporation arranged a sale of German goods to a purchaser in the United States, and title to the goods passed to the purchaser in Europe, as when goods were sold F.O.B. Bremerhaven, no U.S. source income arose.[18]) If a U.S. branch of a foreign bank arranged a loan to a foreign borrower, no U.S. tax was payable on interest paid by that borrower, even though the funds for the loan were provided by the New York agency.[19])

The potential for abuse inherent in these results situations led to one of the most important changes made by the Act, i.e., the extension of the reach of United States taxation to income from sources outside the United States attributable to a business carried on through an office or fixed place of business within the United States by a foreign taxpayer.

13) The effects of "force of attraction" could in some cases be advantageous to the foreign corporate taxpayer. For example, losses of a manufacturing operation would reduce the tax otherwise payable on investment income. Dividends received from United States corporations by an "ETB" foreign corporation were entitled to the dividends received credit which reduced the effective rate of tax on the dividends to 7 ½ percent.

14) Reg. § 1.882-2(b). Certain types of gains from sales of timber, coal and domestic iron ore and gains from sales of preferred stock issued as stock dividends or in the course of reorganizations were also subject to this 30 percent tax. I.R.C. (pre-FITA) §§ 881(a), 306(f).

15) I.R.C. (pre-FITA) §§ 861-864.

16) Elston Co., Ltd., 42 B.T.A. 208 (Non Acq.), appeal to 4th Cir. dismissed Feb. 3, 1941.

17) Reg. § 1.861-7(c).

18) Ibid.

19) I.R.C. (pre-FITA) §§ 861, 862; Reg. § 1.861-2.

B. *The Foreign Investors Tax Act*

As amended by the Act, the Code continues to separate foreign corporate taxpayers into those engaged in trade or business in the United States and those not so engaged. Important changes have been made in the taxation of both groups of taxpayers.

In the case of taxpayers not engaged in trade or business[20]) certain types of income not formerly subject to taxation by the United States are now subject to taxation at the 30 percent (or lower treaty) rate.[21]) These consist of so-called "original issue discount" on debt obligations of United States corporations issued after September 28, 1965, and payments for the purchase of patents, copyrights and other intangibles where the purchase price is contingent upon the productivity, use or disposition of the property purchased.

Two basic changes have been made in the taxation of foreign corporations which are engaged in trade or business. First, in keeping with the recommendations of the Fowler Task Force Report, the scope of application of the "force of attraction" principle has been greatly reduced. Interest, dividends and other "fixed or determinable annual or periodical income" not "effectively connected" with a U.S. trade or business will hereinafter be taxed at 30 percent, rather than at regular U.S. tax rates, as was the case under prior law.[22]) Capital gains which are not "effectively connected" will be free of tax.

The second major change is that foreign corporations which are engaged in trade or business through a U.S. office or fixed place of business must henceforth pay full United States tax on three classes of income from sources outside the United States, where that income is attributable to the office or fixed place of business. The three classes of income are: 1) Gain from sales of inventory property; 2) rents, royalties and gains from sales of patents, copyrights and other intangibles derived in the active conduct of a business; and 3) dividends, interest and gains from the sale of securities derived in the course of an active banking, finance or similar business or by a corporation whose principal business is that of trading in securities for its own account.[23])

Important changes have also been made in connection with the application of the personal holding company tax to foreign corporations and the taxation of dividends and interest paid by foreign corporations.[24])

Since the concept of "engaged in trade or business" occupies such a central place in the scheme of taxation both before and after the Act, we will pause here to discuss its content, or perhaps more properly, its relative absence of content.

III. ENGAGED IN TRADE OR BUSINESS IN THE UNITED STATES

Although the concept of "engaged in trade or business in the United States" has been

20) This phrase and the phrase "not engaged in trade or business" are used hereinafter to refer in each case to the United States.

21) I.R.C. § 882(a). See text at note 51, infra.

22) I.R.C. § 881(a). See text at note 60, infra.

23) I.R.C. §§ 882(a), 864(c)(4). See text at note 93, infra.

24) See text at notes 138-144, infra.

utilized in connection with the taxation of foreign persons at least since 1936,[25]) its content is to this day surprisingly vague.[26]) It is certain, however, that the concept is different from the treaty concept of "permanent establishment," so that a foreign corporation may be engaged in business, but not necessarily through a permanent establishment.[27])

A time element is involved in the determination of whether a taxpayer is "engaged in trade or business," for the taxpayer's status depends on his being engaged in trade or business "at any time" within the taxable year.[28]) If a taxpayer is ETB at any time during the taxable year, the tax results are exactly the same as if it had been so throughout the year.[29]) On the other hand, if the taxpayer is not engaged in trade or business within the taxable year in which income accrues or is received, the implication in the Code and Committee Reports is strong that such income, actually earned in a prior year when it was engaged in trade or business, will be treated as if the taxpayer was not engaged in trade or business.[30])

Turning to the question of what activities will constitute engaging in trade or business by a foreign corporation, a taxpayer who renders personal services such as engineering, product design, or other consultation services in the United States is engaged in trade or business in the United States.[31]) A corporation can supply "personal" services within the meaning of this definition.[32])

As to other activities, however, the concept of "engaging in trade or business" implies some level of continuing activity within the United States. A single transaction or a few sporadic transactions would not cause a foreign taxpayer to be engaged in trade or business in the United States. This, at least, is the teaching of the cases,[33]) although the Internal Revenue Service has indicated that it is its position that a single business venture within the year can constitute "engaging in trade or business."[34]) Despite the position taken by the Service, the better view is that engaging in trade or business has implicit in it the idea of continuing activity. Of course, activity in connection with a single large project, which is in itself a major enterprise, may constitute engaging in trade or

25) Revenue Act of 1936, § 231.
26) See, Garelik, What Constitutes Doing Business Within the United States by a Non-Resident Alien Individual or a Foreign Corporation, 18 Tax Law Rev. 423 (1963); Roberts & Goldberg, Engaged in Trade or Business and H.R. 13103, 24 J. Taxation 364 (1966); Ekman, Tax Problems of Non-resident Aliens, 18 N.Y.U. Institute on Federal Taxation 845, 857 (1960); Saunders, "Trade or Business"—Its Meaning Under the Internal Revenue Code, U.S.C. 12th Annual Institute on Federal Taxes 693 (1960); Comment, U. Chicago L. Rev. 111 (1955).
27) See, e.g., Inez de Amodio, 34 T.C. 894, 909 (1960), affirmed 299 F. 2d 623 (3rd Cir. 1962).
28) I.R.C. § 882(a).
29) Jules Samann, 36 T.C. 1011 (1961).
30) I.R.C. § 881(a); H.R. Rep. 87; S. Rep. 32.
31) I.R.C. § 864(b).
32) British Timken Limited, 12 T.C. 880 (1949), Acq. 1949-2 C.B. 1; Rev. Rul. 60-55, 1960-1 C.B. 270.
33) European Naval Stores Co., S.A., 11 T.C. 127 (1948), Acq. 1948-2. C.B. 2; Continental Trading, Inc., 16 TCM 724 (1957), aff'd 265 F. 2d 40 (9th Cir. 1959); Jorge Pasquel, 12 TCM 1431 (1953); Spermacet Whaling & Shipping Co., S/A, 30 T.C. 618 (1958), aff'd 281 F. 2d 646 (6th Cir. 1960).
34) Rev. Rul. 58-63, 1958-1 C.B. 624 (racehorse entered in a single race), modified on another issue, Rev. Rul. 60-249, 1960-2 C.B. 264.

business.[35]) Quite obviously, the maintenance of a factory, refinery, warehouse or shipping facility would constitute engaging in trade or business.

Continuing activity with respect to the sale of personal property by employees within the United States clearly constitutes engaging in trade or business. Sales activity carried out by an agent would make his principal engaged in trade or business,[36]) even if the agent were an "independent" agent.[37]) It would certainly also be the position of the Service that regular and active solicitation of business in the United States would be sufficient to constitute engaging in trade or business, even though no stock of goods was held in the United States and orders could not be accepted there.[38]) Moreover, cases in a related area indicate that a relatively low level of regular collection and servicing activity within the United States in connection with (1) sales therein, or (2) maintenance of relationships with customers or licensees, even though through an independent agent, may well constitute engaging in trade or business.[39])

It is still unclear whether mere purchasing activity in the United States constitutes engaging in trade or business in the United States.[40])

The maintenance in the United States of the head office of a foreign corporation would probably lead to a conclusion that the corporation was engaged in trade or business there. On the other hand, the performance of mere clerical or ministerial acts within the United States, where the principal management was outside the United States, would not give rise to such a characterization.[41])

The Code specifically provides that a foreign corporation is deemed to be engaged in trade or business in the United States if either a partnership of which it is a partner, or a trust of which it is the beneficiary, is so engaged.[42]) The definition of a partnership includes a "syndicate, group, pool, joint venture, or other unincorporated organization through which . . . any business, financial operation, or venture is carried on."[43]) Thus, for instance, a Canadian livestock dealer who purchased cattle which he shipped to an

35) See Roberts & Goldberg, supra, at 356; see also the dissenting opinion in Spermacet Whaling 281 F. 2d 646, at 652.

36) See Rev. Rul. 55-617, 1955-2 C.B. 774; G.C.M. 21219, 1939-1 C.B. 201 (exclusive United States agency to commission agent); but see Estate of B.W. Cadwallader, 13 T.C. 214, 220 (1949).

37) See Frank Handfield, 23 T.C. 633 (1955); Rev. Rul. 55-617 supra; *cf.* Inez de Amodio, 34 T.C. 894 (1960), aff'd as to other issues, 299 F. 2d 623 (3rd Cir. 1962); Jan Casimir Lewenhaupt, 20 T.C. 151 (1953), aff'd, per curiam, 221 F. 2d 227 (9th Cir. 1955).

38) Rev. Rul. 62-31, 1962-1 C.B. 367;
Rev. Rul. 56-165, 1956-1 C.B. 849.

39) See, e.g., Jan Casimir Lewenhaupt, supra.

40) I.T. 1406, I-2 C.B. 151 (1922). (Regular purchases by purchasing agent constitutes doing of business); T.D. 3111, 4 C.B. 280 (1921). (Mere buying of goods with capital from abroad to be sold abroad is not a trade or business in the United States); see Balanovski v. Commissioner, 131 F. Supp. 898 (D.C. N.Y. 1955), aff'd in part, reversed in part, 236 F. 2d 298 (2nd Cir. 1956).

41) See Spermacet Whaling, supra. Note that in the Spermacet case the Service contended unsuccessfully that relatively minor administrative acts in the United States led to the corporation's being engaged in trade or business. See also Consolidated Premium Iron Ores, Ltd., 28 T.C. 127 (1957), aff'd 265 F. 2d 320 (6th Cir. 1959) where a similar contention was unsuccessfully made.

42) I.R.C. § 875.

43) I.R.C. § 7701(a)(2).

American dealer who sold the cattle in the United States for their joint profit or loss was held to be engaged in trade or business in the United States and so taxed.[44])

To summarize, any continuing level of activity by employees or agents of a foreign corporation in the United States is likely to result in a holding that the corporation is engaged in a trade or business in the United States, if these activities lead to or are ancillary to the manufacture, or sale, of property, or to the rental or licensing of equipment, patents or other intangibles in the United States. This conclusion may well be reached under the Code, even if the agent is "independent." Regular purchasing activities in the United States through a United States employee or agent may also cause the corporation to be engaged in trade or business, although this point is not entirely clear. Continuing supervision and general management of a corporation's activities will also probably lead to a holding that the corporation is so engaged. A foreign corporation engaged in trading in securities for its own account will not be considered engaged in trade or business unless its principal office is in the United States.

IV. TAXATION OF FOREIGN CORPORATIONS NOT ENGAGED IN TRADE OR BUSINESS IN THE UNITED STATES

The Act provides a relatively simple scheme of taxation for corporations not engaged in trade or business in the United States. A flat 30 percent (or lower treaty) tax is imposed on certain types of income. All other income from sources within and without the United States is free of United States tax.[45]) Thus, for instance, if a foreign corporation not engaged in trade or business purchases a shipload of oil in Venezuela which it sells in the United States, with title passing F.O.B. New York, the income therefrom would not be subject to tax in the United States even though the "source" of this income is considered to be in the United States.

The largest and most important class of income which is subject to withholding tax consists of a category defined by the Code as "interest, dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, and other fixed or determinable annual or periodical gains, profits and income," such as royalties.[46]) This is a tax on gross income without any allowance of deductions for related expenses or for recovery of capital costs.[47]) The definitions of these types of income are, of course, those supplied by the internal tax law of the United States.[48])

44) W. C. Johnston, 24 T.C. 920 (1955).
45) I.R.C. § 881.
46) I.R.C. § 881(a)(1). Reg. § 1. § 871-7(b) (2).
47) The Code however permits taxpayers to elect to be taxed on a net basis at regular rates on income from real property. I.R.C. § 882(d). The election is similar to the election permitted by the treaties (e.g., U.S.-Germany Income Tax Convention Art. IX; U.S.-United Kingdom Income Tax Convention Art. IX), but differs in important details.
48) Thus, for instance, gain upon sales or redemptions of certain preferred stocks issued as stock dividends or in the course of a reorganization by a domestic corporation is subject to tax as if a dividend had been received at the time of such sale or redemption. I.R.C. § 306(f). Interest is "imputed" in certain cases where no stated interest charge is provided for in connection with deferred payments

A foreign taxpayer receives the benefit of any exemption from tax available to domestic taxpayers, such as the exemption from tax on interest paid by states, territories and their political subdivisions.[49]) Interest paid by banks to foreign corporations not engaged in trade or business is exempt from tax and will remain so until December 31, 1972.[50]) Thereafter this interest will be subject to tax. However, we believe it doubtful that this change will come into effect in view of its potentially serious adverse effect on the United States balance of payments.

The Code subjects to the 30 percent withholding tax three specially defined types of gains: 1) original issue discount; 2) certain gains on sales of timber, coal and domestic iron ore; and 3) certain gains on sales of patents, copyrights and similar intangibles.[51])

So-called "original issue discount" on corporate obligations is, under many circumstances, subject to tax in the hands of a domestic taxpayer as ordinary income, rather than as capital gain upon sale or redemption of the debt obligation. The Act, in a logical extension of this treatment, provides for withholding at the 30 percent rate upon payment of original issue discount on obligations issued by corporations after September 28, 1965.[52]) There may well be serious problems of enforcement in connection with this tax, particularly where the obligations are sold by one foreign taxpayer to another outside the United States. Discount of this type will be treated as "United States source income" and also as interest for the purposes of the various special treaty provisions applicable to interest.[53])

The Code provides for the taxation of certain receipts from the sale of timber, domestic iron ore and coal as capital gain rather than ordinary income, even though the purchase price may be keyed to profit realized on the disposition of the property by its purchaser, or to the number of units extracted. The net amount of gain upon such payments received by a foreign taxpayer is subject to withholding at 30 percent.[54])

Perhaps the most radical change in this area is the imposition of a 30 percent withholding tax upon gains from sales[55]) after October 4, 1966 of patents, copyrights, secret processes and formulae, good will, trademarks, trade brands, franchises and like property, and any interest in such property (referred to hereinafter as "intangibles"), to the

arising out of a sale of property. I. R. C. § 483. The imputed interest portion of any such payment to a foreign corporation would be subject to withholding tax at the statutory rate of 30 percent, or to a lower treaty withholding rate where applicable.

49) I. R. C. § 103.

50) I.R.C. § 861(c).

51) I. R. C. § 881(a)(2), (3), (4).

52) I. R. C. § 881(a)(2).

53) T. I. R. 887 (December 28, 1966). Interest and original issue discount on bonds of overseas financing subsidiaries of United States corporations will generally be exempt from all United States withholding tax since interest paid by such corporations generally will not constitute United State source income. I. R. C. § 861(a)(1)(b).

54) I. R. C. §§ 881(a)(3), 631(b), (c); Reg. § 1.1441-2(b).

55) As to the distinction between a license upon which "royalties" are payable and a sale which gives rise to "gain" for United States tax purposes, see Rev. Rul. 60-226, 1960-1 C. B. 26; Rev. Rul. 58-353, 1958-2 C. B. 408; Rev. Rul. 54-409, 1954-2 C. B. 174; Cooper, Tax Aspects of Corporate Exploitation of Inventions and Know-How, 38 So. Calif. L. Rev. 6 (1965); Duke, Foreign Authors and Inventors and the Income Tax, 72 Yale L.J. 1093 (1963).

extent that the gain is from payments which are "contingent on the productivity, use or disposition of the property or interests sold or exchanged."[56]) Gain realized upon a "sale" for a fixed price, even though payable in installments over a period of years, will not be subject to any United States tax if payable to a foreign corporation not engaged in trade or business.[57]) If part of such a payment received during a year is fixed and part contingent, the contingent portion will be subject to a 30 percent United States tax, and the non-contingent portion will not be subject to tax. However, if more than 50 percent of the gain for any taxable year from such a sale is from payments which are contingent, then the entire payment will be treated as being from payments which are contingent and, therefore, subject to tax.[58]) If the sale of the intangible took place prior to October 5, 1966, gain recognized in the years to which the Act is applicable will be free of United States tax so long as the foreign corporation is not engaged in trade or business.

Although there is some question as to whether payments in connection with a "sale" of such intangibles would be considered "royalties" for purposes of the various treaty preferences and exemptions, the Report of the Senate Committee suggests that they would be,[59]) but the matter will not be clear until the Treasury Regulations appear.

V. CORPORATIONS ENGAGED IN TRADE OR BUSINESS IN THE UNITED STATES

A foreign corporation which is engaged in trade or business is taxable at the ordinary corporate rates applicable to domestic taxpayers upon all income that is "effectively connected" with that trade or business. The Code then provides different tests for determining whether each of three different types of income are "effectively connected" with the United States trade or business. One test is applicable to periodical income and capital gains from sources within the United States; a second applies to all other United States source income, and a third is applied to certain types of foreign source income.

To eliminate the "force of attraction" principle inherent in prior law the Code now allows the foreign taxpayer to divide his United States source income into two segments. One of these consists of what might loosely be termed "periodical income and capital gains," i.e., dividends, interest, rents, royalties, gains from the sale of capital assets and other income which would either be taxed at 30 percent rates or be exempt from tax, if received by a foreign taxpayer not engaged in trade or business.[60]) The other segment

56) I.R.C. § 881(a)(4).

57) Note that a portion of such payments may, under certain circumstances, be considered to be "imputed interest" upon which a withholding tax would be payable. I.R.C. § 483.

58) I.R.C. §§ 871(e), 881(a)(4).

59) S. Rep. 24, 41. It is also possible that such payments may be entitled to the exemption provided for sales of capital assets under certain of the treaties. E.g., United States-Canada Income Tax Convention, Article VIII. See United States-Germany Income Tax Treaty Article VIII which exempts gains from sales of intangibles from taxation.

60) See part IV of this paper.
I.R.C. §§ 864(c)(2), 881.

consists of all other income from sources within the United States.[61]) To the extent that periodical income and gains from the sale of capital assets are effectively connected with a United States trade or business they are taxed as if received by a United States corporation.[62]) To the extent not so effectively connected, periodical income and capital gains are taxed as if received by a taxpayer not engaged in trade or business within the United States.[63]) All other income from sources within the United States is treated as effectively connected and hence subject to full United States tax.[64]) In addition, the Code treats as effectively connected three specified types of income from sources without the United States to the extent that they are attributable to an office or fixed place of business in the United States.[65])

The statutory technique for granting favorable treatment to periodical income and capital gains is somewhat less generous than the declared policy of eliminating the force of attraction principle. Under the act, once a taxpayer is engaged in trade or business in the United States all income from sources within the United States is taxed at the rates applicable to domestic taxpayers, unless such income falls within the exception for periodical income or capital gains which are not effectively connected. Because the burden of proof in United States tax litigation is generally on the taxpayer, the force of attraction concept is still present in the procedural sense that once a corporation is engaged in business in the United States, all U.S. source income will be taxed at full rates unless the taxpayer can satisfy the burden of proving that periodical income and capital gain is not effectively connected with the business.

Force of attraction also persists in another sense. Because all income other than periodical income or capital gains is automatically effectively connected, other types of United States source income will be fully subject to United States tax even if they have no relationship to the taxpayer's United States trade or business. Thus, if a foreign corporation engaged in the business of selling radios through a New York office is also engaged in manufacturing automobiles in Japan and makes a shipment of automobiles which it sells F.O.B. San Francisco, the sale will be fully subject to United States tax even though the New York office played no part in the sale.

Assuming that a foreign corporation has "effectively connected" income, it is entitled to deduct in computing its tax only those expenses "connected" with that income.[66]) Very little authority exists as to what deductions will be regarded as "connected."[67])

61) I.R.C. § 864(c)(3).

62) If the United States trade or business does not constitute a permanent establishment such income may still be entitled to taxation at reduced rates under applicable income tax conventions.

63) I.R.C. § 881. The existence of a United States permanent establishment is to be ignored in determining the treatment of periodical income or capital gains under the treaties unless the income is effectively connected with the permanent establishment. I.R.C. § 894(b).

64) I.R.C. §§ 864(c)(3), 881.

65) I.R.C. § 864(c)(4). These are the common cases. A foreign insurance company engaged in trade or business in the United States is also taxed on any foreign source income "attributable" to its United States trade or business. I.R.C. § 864(c)(4)(C).

66) I.R.C. § 882(c)(1)(A). Charitable contribution deductions are allowed without this limitation. I.R.C § 882(c)(1)(B).

67) Some guidance can be gleaned from the proposed regulations issued under I.R.C. § 482. Prop. Reg. §§ 1.482-1, 1.482-2.

It should be noted that deductions are allowed in computing taxable income only if a "true and accurate" return has been filed.[68]) No foreign tax credit is allowed except with respect to certain foreign taxes imposed on income from without the United States that is treated as effectively connected.[69])

A. *Determining Whether Periodical Income and Capital Gains are "Effectively Connected" Income*
The statute does not precisely define the phrase "effectively connected", as it is used in connection with periodical income and capital gain but instead gives three general tests for use in determining whether items of such income have that generally disadvantageous status.[70]) The first is a "use test": whether the item is "derived from assets used in or held for use in the conduct of" the U.S. enterprise.[71]) The second is an alternative "activity test": whether the activities of the United States business "were a material factor in the realization" of the income, gain or loss in question.[72]) The third is an accounting standard: in applying the first two tests "due regard" must be given to whether or not the item of income was accounted for through the books of the United States business.[73]) The incorporation of the place of accounting standard undoubtedly means as a practical matter that anything about which there could be a dispute will be accounted for outside the U.S., thereby adding to the difficulties of decision and enforcement in precisely those cases which are likely to present enforcement problems.

The legislative committee reports provide some helpful practical discussion of the concepts involved in the three tests. They state that "effectively connected" implies a "direct relationship" between the asset and the business:[74]) Thus, where a foreign corporation invests in stock of a United States vendor in order to assure a source of supply for its United States business, dividends and gains from that stock will be treated as effectively connected.[75]) Similarly, short term investment on a seasonal basis in the United States of surplus business funds will give rise to effectively connected assets, income, gains, and the like.[76]) Interest on overdue accounts receivable of the United States business would be subject to the ordinary, rather than the reduced flat rates of tax.[77]) The exemption available to foreign depositors until 1973[78]) with respect to interest paid by domestic banks is unavailable where such deposits are effectively connected with a

68) I.R.C. § 882(c)(2).
69) I.R.C. §§ 882(c)(3), 906.
70) See discussion at H.R. Rep. 58; S. Rep. 17. Note that the taxpayer may, as under prior law, on occasion want income to be "effectively connected.".See note 13 supra.
71) I.R.C. § 864(c)(2)(A).
72) I.R.C. § 864(c)(2)(B)
73) I.R.C. § 864(c)(2).
74) H.R. Rep. 59:
"If there is no direct relationship between the U.S. business and the holding of the asset, such asset will not generally be considered used in, or held for use in, such business, and the income from such asset will not be considered effectively connected with the conduct of such business."
See also S. Rep. 20-21.
75) H.R. Rep. 59.
76) H.R. Rep. 60.
77) H.R. Rep. 60.
78) I.R.C. § 861(c).

business conducted by the deposit or in the United States that exemption is inapplicable.[79])

The House Committee Report states that in applying the "use test," consideration is to be given primarily to the needs of the business in the United States. Also to be taken into account are (1) the source of the funds used to acquire the asset in question (whether from the United States business or from abroad); (2) the disposition of the income from the asset (whether or not it is retained for use in the United States business); and (3) the extent of management or control of the asset exercised by the United States business. If the last three factors are sufficiently persuasive, items may be considered effectively connected even if no need for the asset by the United States business is shown.[80])

The "activity test" will be of primary significance in the case of periodical income where the taxpayer is engaged in the United States in a financial, banking or similar business, or a licensing or real estate business, and the income arises from such activities. On the other hand where the foreign corporation is engaged in manufacturing, or distributing merchandise, for example, activity by its officers in connection with portfolio investment will not convert that portfolio into effectively connected assets unless the maintenance of investments is the "principal activity" of the corporation.[81])

The Committee Reports make it clear that portfolio investments in the United States by foreign taxpayers do not give rise to effectively connected income, even where the investments are attributable to surplus profits of the United States business, are paid in the first instance into the U.S. business and are managed by the officers of the U.S. branch, so long as the investment and the income therefrom are not used in or needed by the business.[82]) Moreover, a domestic subsidiary corporation whose stock is carried on the books of a United States branch as an asset would not be deemed to distribute effectively connected dividend income where its business was unrelated to that of the branch, and its management reported to its parent abroad rather than to the United States branch.[83])

The relation of portfolio investments to the "needs of a business" seems likely to produce some delicate questions. For example, suppose that the branch of a foreign corporation conducts an active business in the United States and makes large borrowings from a United States bank to take care of seasonal needs. Suppose further that the corporation maintains portfolio investments in marketable securities deposited with the same bank. Does the fact that the bank, under typical American bank documents, has the right to look to the portfolio securities to collect its loans mean that such investments are "effectively connected" because of the indirect relationship to the credit of the business? If so, one must conclude that all of the assets of a foreign corporation held by a creditor bank in the United States are "effectively connected" when the United States business of that corporation avails itself of domestic banking facilities even

79) Ibid. See H.R. Rep. 60. This may in many cases have an effect contrary to the policy objective of improving the United States balance of payments. A foreign taxpayer is free to invest surplus funds outside of the United States, for example, by the purchase of certificates of deposit issued by a non-U.S. bank or by a foreign branch of a U.S. bank, thereby avoiding the U.S. tax at full rates on "effectively connected" interest income.

80) H.R. Rep. 59.

81) H.R. Rep. 58-61; S. Rep. 19-21.

82) H.R. Rep. 60-61.

83) H.R. Rep. 61.

though such assets are not specifically pledged. This result would be unfortunate, but can be easily avoided by the use of foreign banking facilities. It is our conclusion that borrowing in the U.S. by a foreign taxpayer engaged in business herein does not "effectively connect" U.S. investments held by the lender as custodian, for the connection is too indirect. On the other hand, if the investment account was actually pledged to secure the seasonal borrowings, there would then be a more direct relationship to the needs of the business, and the result might well be a finding of "effective connection."

A principal criticism of section 864(c) during the period when the FITA was under consideration in the Congress was the asserted vagueness of the "effectively connected" concept.[84]) Indeed, some of the imprecision seems almost deliberate. The "use" and "activity" tests, for example, are not conclusive, but merely are "among the factors" to be included in determining whether an item is effectively connected. The "other factors" were apparently meant to be those mentioned in the legislative history of the Act. The accounting factor is not decisive; it need be given only "due regard." But there is no indication of how much regard is due. The Administration proponents of the bill conceded that there was a residue of uncertainty on the fringe of the concepts involved, but asserted that the bill was sufficiently clear to answer the questions which would arise in the bulk of practical cases.[85])

The phrase "effectively connected" is derived from the OECD Model Income Tax Convention and conforms to the approach followed by the U.S. in its more recent tax treaties with the United Kingdom, Germany and The Netherlands. The use of the term

84) See, e.g., the following exchange between Senator Dirksen, Secretary of the Treasury Fowler, and Asst. Secretary Surrey:
"*Senator Dirksen:* Mr. Secretary, I have one question. All the representations and all the mail I have received concern section (2)(c)(1) on page 12. The words are "effectively connected." They point out that foreign corporations doing business in this country but, at the same time, out of their home office in their own country they do an investment business, but they permit their New York office to collect a return, interest and principal, on foreign loan repayments and so forth. They are uneasy about what the interpretation of the proposed "effectively connected" is going to be. I have had mail from Asia, Europe, and any number of people in this country, and I swear that all the letters deal with just that item. I understand that it is on page 12 of the bill.
"*Secretary Fowler:* Yes, Senator Dirksen, this has been a phrase that has given rise to some concern . .
"*Mr. Surrey:* It is a phrase [effectively connected] which we are now using in our treaties with the Western European countries in conformity with the model draft which the OECD has written. We are extending it in this bill to all of the countries without waiting for treaties on this particular point. Now, it is a new phrase in our tax language, and, consequently, there will be doubts at the borderline until some more experience is gained . . .
"*Senator Dirksen:* Would it be advisable to expand the definition in the statute itself so that they would be fully on notice without having to depend on any Treasury regulations?
"*Mr. Surrey:* If the language could be found, Senator. It is like the situation today where, for example, we use the phrase "engaged in trade or business in the United States." It is rather hard to expand upon language of that nature. It takes time to gain experience with the borderline cases. The phrase "effectively connected" is defined to some extent in the statute on page 13, so that there are some guides there.
"We would not be adverse to improving the language in the bill or to adding language in the committee report if it would give people more guidance." Hearings Before the Senate Committee on Finance on H.R. 13103, 89th Cong. 2d Sess. 51-52 (1966).

85) Ibid.

has the advantage of consistency with international practice but there is little authority outside the United States as to its meaning. The statute at any rate illustrates the difficulty of establishing general verbal formulae for matters which can only be understood in specific terms, which is to say on a case-by-case basis.

There is existing United States case law pertinent to the interpretation of the phrase "effectively connected." The cases arise primarily in connection with the distinction between proporties which are treated as capital assets, and those which are not so treated. Gains on sales of capital assets are taxed at lower than ordinary rates, but losses are allowable only as offsets to capital gains.[86])

One leading case involved gains from the sale of grain futures by a grain processor who held these futures as "hedges" against its future milling requirements. The Supreme Court held the assets not to be capital assets because of the close connection between the hedging transactions and the main stream of the taxpayer's business, although the futures contracts fell squarely within the literal statutory definition of a capital asset.[87]) Another line of cases holds that losses from sales of securities acquired to support failing vendors or customers, or to assure sources of supply, are deductible as ordinary rather than capital losses, despite the fact that the securities come within the literal definition of "capital assets," because of their close relationship with the corporation's ordinary business.[88])

It seems clear from these cases where assets have been held not to constitute capital assets in the hands of domestic taxpayers, that analogous items would be held to be effectively connected and taxed at ordinary income tax rates in the hands of a foreign corporation.

However, in many cases where gain from the sale of an asset is taxed as capital gain to a domestic taxpayer, the foreign taxpayer will be similarly taxed. The reason for this lies in the fact that the Code allows capital gain treatment to gains on the sale of many assets which are unquestionably "effectively connected" with a taxpayer's business. This may occur in connection with occasional dispositions of machinery, real estate and buildings used in the taxpayer's business, but not held for sale to customers,[89]) or in connection with earmarked portfolio securities of a taxpayer engaged in the securities business as a broker-dealer because of the relationship between the earmarked securities and the capital requirements of the business.

86) I.R.C. §§ 1201, 1212.

87) Corn Products Refining Co. v. Commissioner, 350 U.S. 46 (1955). See also Albert Kurtin, 26 T.C. 958 (1956); Wool Distributing Corp. 34 T.C. 323 (1960); Fulton Bag & Cotton Mills, 22 T.C. 1044 (1954); Weiler v. U.S., 187 F. Supp. 742 (M.D. Pa. 1960); U.S. v. Rogers, 286 F. 2d 277 (6th Cir. 1961). *Cf.* Rev. Rul. 58-40, C.B. 1958-1.

88) See Mansfield Journal Co. v. C.I.R., 274 F. 2d 284 (6th Cir. 1960); C.I.R. v. Bagley & Sewall Co., 221 F. 2d 944 (2d Cir. 1955); Tulane Hardwood Lumber Co., Inc. v. C.I.R., 24 T.C. 1146 (1955); Arlington Bowling Corp. v. C.I.R., T.C. Memo 1959-201 (1959); Helen M. Livesley, T.C. Memo 1960-24 (1960); Edwards v. Hogg, 214 F. 2d 640 (5th Cir. 1954); Journal Company v. U.S., 195 F. Supp. 434 (E.D. Wis. 1961). But *cf.* Gulftex Drug Co., 29 T.C. 118, aff'd 261 F. (2d) 238 (5th Cir. 1958), (sale long after original purpose of acquisition had ended. Held stock deemed to be investment, and loss on sale was capital loss). See also Philip W. Fitzpatrick, 26 C.C.H.T.C.H. 1(1967) 1967-1, and cases cited therein, dealing with loans by corporate officers to their employers.

89) I.R.C. § 1231.

One question on which there is no significant precedent or aid from the Committee Reports is as to the consequences of the liquidation of a corporation or the sale of a business. What is the effect of liquidation of a subsidiary corporation by a foreign parent which then proceeds to carry on the business through a United States branch? It might be argued under the language of section 864(c)(2) that the gain was derived from assets (i.e., the proceeds of the corporate liquidation) held for use in the conduct thereafter of the business, and thus that the liquidation gain was taxable as "effectively connected." The correct result in such a case would seem to be that the asset from which the gain was derived was the capital stock of the subsidiary, which was not used or held for use in connection with the ongoing trade or business after liquidation of the subsidiary. It may also be possible under existing Code provisions in such cases to obtain rulings prior to the liquidation that gain is taxfree.[90] However, the Service may make the payment of a dividend tax on the amount of the accumulated earnings and profits of the subsidiary a condition of issuing such a ruling.[91]

Upon the sale of an entire business carried on as a branch, the gain will be fragmented into various elements and separately treated.[92] Gain from sales of inventory or assets held primarily for sale to customers would be taxed as ordinary income. Gain from the sale of machinery, land and depreciable real property used in the business will be taxed at capital gains rates. Although some question may exist as to whether good will, trade marks and tradenames are "effectively connected" and would be considered "used" in connection with a terminated business, the more likely interpretation is that gain from the sale of such assets is indeed "effectively connected", and hence subject to capital gains tax.

B. *Income From Sources Without the United States Attributable to an Office or Fixed Place of Business in the United States*

The Act subjects to tax in the same manner as if earned by a United States corporation certain income which is attributable to a United States office or fixed place of business, but which is from sources without the United States. This extension of taxing jurisdiction applies with respect to three specified types of income: 1) rents and royalties from the use of patents, copyrights, secret processes and formulas, good will, trademarks, trade brands, franchises and other like properties, and gain from the sale of such intangibles derived in the active conduct of a trade or business within the United States; 2) dividends or interest, or gain from the sale, of stock, notes, bonds, or other evidences of indebtedness derived in the active conduct of a banking, financing or similar business, or received by a corporation whose principal business is trading in securities for its own account; and 3) income from sales of personal property.[93]

90) See I.R.C. § 332 which provides that no gain or loss shall be recognized upon complete liquidation of a subsidiary. But see I.R.C. § 367 which provides in effect that such tax free status is not to be available unless it is established by ruling of the Internal Revenue Service prior to the liquidation that the liquidation is not in pursuance of a plan having as one of its principal purposes avoidance of income taxes.

91) Announcement 66-33, 1966-40 I.R.B. 17 (Oct. 3, 1966) sets forth proposed guidelines regarding transactions requiring advance rulings under § 367.

92) Williams v. McGowan, 152 F. 2d 570 (2d Cir. 1945).

93) I.R.C. § 864(c)(4).

According to the Committee Reports this extension of taxing jurisdiction was enacted because of a fear that the United States was in some cases being used as a tax haven.[94]) This might occur, for instance, where a foreign country did not tax its domestic corporations on income from the conduct of business outside the country. In such cases a sale of goods to countries other than the United States or the country of incorporation by a sales office located in the United States was in many cases free of all tax. In actuality, these provisions were probably aimed in large part at subsidiaries of domestic corporations, which, because of the nature of their operations, fell outside the scope of the controlled foreign corporation provisions of the Revenue Act of 1962.

This extension of taxing jurisdiction applies only to a corporation which has an "office of fixed place of business" within the United States.[95]) If the corporation is ETB, but not through an office or fixed place of business, no foreign source income will be taxable.[96]) We will therefore first explore that concept, and then discuss the three types of income from sources without the United States that are now subject to taxation by the United States.

1. The Definition of an "Office or Fixed Place of Business"

It is quite likely that the concept of "office or fixed place of business" will be interpreted to have a content very close to that of the concept of "permanent establishment" used in income tax treaties.[97])

Some idea of the content of this concept can be gathered from two existing bodies of authority: U.S. court decisions as to the meaning of the term "permanent establishment"; and judicial interpretations of the term "office or fixed place of business" which appeared in the Code before 1942. The court decisions concerning the existence of a permanent establishment state that the concept implies the existence of an office and staff capable of carrying out the day-to-day business of the corporation and its use for such purpose, or that it suggests the existence of a plant or facility equipped to carry on the ordinary routine of such business activity.[98])

The Internal Revenue Service has ruled that much less substantial contacts with the United States, e.g., a race horse in the country for several races, or traveling salesmen demonstrating logging equipment over an extended period, may constitute a "permanent establishment."

The cases interpreting the concept of office of fixed place of business suggest that if relatively minimal clerical functions are exercised in the United States, no office or fixed place of business exists.[99]) However, in a case where the foreign corporation actually

94) H.R. Rep. 14; S. Rep. 18.
95) I.R.C. § 864(c)(4)(B).
96) I.R.C. § 862(c)(4)(A).
97) S. Rep. 1707 at p. 20 asserts that with respect to the language of § 864 (c)(5)(A), relating to agents in the United States, the Code is substantially similar to the content of the treaties.
98) See, e.g., Consolidated Premium Iron Ores, Ltd., 28 T.C. 127 at 152 (1957), non-acq. 1958-1 C.B. 7, aff'd 265 F. 2d 320 (6th Cir. 1959).
99) Linen Thread Co. Ltd. v. Comm'r., 128 F. 2d 166 (2d Cir. 1942); Aktiebolaget Separator v. Hoey, 49-1 USTC Par. 9253 (1949).

established a functional office in this country with an assistant secretary present, and the office kept records with respect to the taxpayer's transactions and stockholdings, collected dividends, prepared reports for the home office, prepared tax returns and generally took care of the taxpayer's affairs in the United States, including the investigation of proposed reorganizations of corporations in which the foreign corporation held securities, the corporation was held to have an office or fixed place of business in the United States.[100])

Starting with this fairly scant body of authority certain conclusions can be drawn. The existence of a branch office, factory, workshop or mine in the United States would clearly constitute an office or other fixed place of business. A warehouse would probably constitute a fixed place of business. A showroom would also constitute a fixed place of business, even if the employees of the showroom did not have the power to conclude sales.[101])

More subtle problems arise once one moves beyond this group of fairly obvious cases. For instance, suppose that a foreign corporation is the wholly owned subsidiary of a United States corporation having its home office in New York. The Committee Reports indicate that the mere fact that the officers of the parent corporation exercise general supervision over the policies of the foreign corporation does not require the conclusion that the subsidiary has an office or fixed place of business in the United States.[102]) Moreover, the fact that the managing director of the foreign subsidiary, who is permanently stationed abroad, occasionally visits the United States and continues to exercise direction over the subsidiary's operations while he is in the United States does not cause the subsidiary to have an office or other fixed place of business in the United States "even though it may be engaged in trade or business within the United States."[103])

The Report then goes on to state that if an employee of the parent corporation "on rare occasions" receives an order which he accepts on behalf of the foreign subsidiary after consultation with officials of the foreign subsidiary, the subsidiary will not be found to have an office or other fixed place of business in the United States because of these activities. This conclusion is limited by a statement that the parent must not hold itself out as a person to be contacted by those wishing to do business with the subsidiary; and that orders are "seldom handled" in this manner and do not constitute a significant part of the subsidiary's business.[104]) However, if an officer of the parent corporation reviews all orders of the subsidiary before acceptance, the report concludes that an office or fixed place of business exists in the United States.[105])

It is therefore obvious that if the general day-to-day management of a foreign subsidiary is supervised from a New York office of its parent corporation or of a person controlling the foreign corporation, the office or fixed place of business of the parent corpo-

100) Scottish American Investment Co., Ltd., 47 B.T.A. 474 (1942).
101) E.g., Rev. Rul. 62-31, 1962-1 C.B. 367.
102) H.R. Rep. 63.
103) Ibid.
104) Ibid.
105) Ibid.

ration will be deemed to be the office or fixed place of business of the subsidiary.

Turning in the other direction, the question naturally arises whether the United States office of a subsidiary of a foreign corporation may constitute the office or fixed place of business of its parent. There is scant authority on this point, and the Committee Reports do not even refer to it. However, the question cannot be ignored, since the Code does not contain a provision similar to that contained in many of the treaties stating that a foreign corporation having a domestic subsidiary "shall not be deemed by reason of such fact to have a permanent establishment in the United States."[106])

One can only conclude at this time that if a U.S. subsidiary actively participates in transactions of the types which may lead to United States taxation of its parent's foreign source income, there is a significant danger that the office or fixed place of business of the subsidiary will be deemed the office or fixed place of business of the parent.[107])

The Code and Committee Reports indicate that under certain circumstances the office or fixed place of business of an "agent" will constitute an office or fixed place of business of his principal. The Code states conditions, somewhat similar to those stated in the Treaties with respect to "permanent establishment" under which a U.S. agent's office will not be considered the office or fixed place of business of his principal. The statutory provision is as follows:

> "(A) in determining whether a nonresident alien individual or a foreign corporation has an office or other fixed place of business, an office or other fixed place of business of an agent shall be disregarded unless such agent (i) has the authority to negotiate and conclude contracts in the name of the nonresident alien individual or foreign corporation and regularly exercises that authority or has a stock of merchandise from which he regularly fills orders on behalf of such individual or foreign corporation, and (ii) is not a general commission agent, broker, or other agent of independent status acting in the ordinary course of his business".[108])

Thus, it is clear that an agent's office will not be considered that of his parent if the agent is of "independent status." There is little authority as to when an agent will be considered "independent." However, the implication from the statutory text is clear that an agent who is not subject to the control of the foreign principal and carries on activities, such as sales activities, for many principals would presumably be "independent."[109] However, if the principal dominated the agent, or was his sole customer, one may doubt that he would be considered to be of "independent status."

The fact that the agent is not "independent" does not conclude the discussion. The agent's office is not the office of his foreign principal unless he either (a) has a stock of goods from which he regularly fills orders on his principal's behalf, or (b) has and regularly exercises an authority to negotiate *and conclude* contracts on behalf of the foreign corporation. Thus, if the U.S. agent, even though not independent, is required to send

106) E.g., U.S.-Canada Income Tax Convention, Protocol § 3(f)(March 4, 1942); Reg. § 519.103(a); U.S.-Luxemburg Income Tax Convention, Art. 2(f)(vi).

107) This is particularly so because of the danger that a subsidiary may be deemed an agent of the parent corporation.

108) I.R.C. § 864(c)(5)(A).

109) C.f. Inez de Amodio, 34 T.C. 894, at 908 (1960), aff'd as to other issues 299 F. 2d 623 (3rd Cir. 1962).

any orders he may solicit abroad for final approval, and if the record shows that approval is a significant condition, then the office of the agent would probably not be considered an office of the principal. A United States court is not likely to find approval to be a significant condition unless the home office on a fairly regular basis questions, modifies and at times rejects proposed contracts.

2. Rents, Royalties and Gains From Sales Of Intangibles

Rents and royalties from the use of intangibles, patents, copyrights, secret processes and formulas, good will, trade marks, trade brands and other like intangible property in countries other than the United States are subject to full United States tax if "attributable" to a United States office of fixed place of business of the taxpayer and derived in the active conduct of a trade or business in the United States.[110]) Similarly, gains from the sale of intangibles which are "attributable" are taxed.[111])

The key question is, of course, under what circumstances such royalties or gains will be "attributable" to a United States office. The Code states that foreign source income will be "attributable" only if activities of the United States office are a "material factor" in producing such income.[112]) Furthermore, the income is to be taxed only to the extent "allocable" to the United States office or fixed place of business.[113])

The meaning of these limitations is explained in the accompanying Committee Reports. They state that to be "material" the activities of the local office must be "significant" and must provide an essential economic element in the transaction. However, these activities need not necessarily be a "major" factor in the production of the income to be "material".[114]) Furthermore, income from a lease, license or sale will not be attributed to a United States office unless the lease, license or contract of sale is made through or by the United States office,[115]) and those types of income will not be attributed to the United States merely because the United States office developed the property in question or exercised "general supervision" over the activities of the persons who made the lease or sale.[116]) Thus, the fact that a laboratory in the United States developed a patent is irrevelant, if a license to a licensee in a foreign country is negotiated by employees of an office outside the United States. In short, sales activities are made the prime determinant of whether United States tax will be assessed. The lease, license or sale is to be treated as made through the United States office if that office actively participates in soliciting, negotiating or performing other activities required to arrange the transaction, or performs significant services incident to the lease or license.[117])

The government's general approach in such cases will probably begin with the premise that if a lease or license is attributable to a United States office all income from the lease

110) I.R.C. § 864(c)(4)(B)(i).
111) Ibid.
112) I.R.C. § 864(c)(5)(B).
113) I.R.C. § 864(c)(5)(C).
114) S. Rep. 21.
115) H.R. Rep. 64.
116) Id. at 65.
117) Id. at 64.

or license is "allocable" to that office and fully subject to taxation in the United States. If the foreign taxpayer's only office or fixed place of business is in the United States, all of his rents, royalties and sales proceeds will "in general" be attributable to that office.[118]) It thus becomes essential in such cases to establish an office or fixed place of business outside the United States if full United States tax upon all the income in question is to be avoided. Where a lease or license is attributable to a United States office it may be possible to reduce the income subject to United States tax by showing that a foreign office made a material contribution to the negotiation of the lease or license or in providing ancillary services in connection therewith.

The Code also states that no income is to be taxed to a United States office unless it regularly carries on activities of the type in question.[119]) Thus, if the United States place of business is not primarily a sales or licensing activity, but occasionally realizes income from licenses abroad, no U.S. tax will be assessed. But a sales office whose primary function is licensing and selling in the United States will attract tax on income from licenses made through it of rights in Mexico and Canada.[120])

3. Dividends, Interest and Gains from Sales of Securities

Dividends, interest and gains from the sales of securities giving rise to foreign source income will be taxable in the United States if attributable to a United States office or fixed place of business, and if realized by one of two types of corporations: a corporation engaged in a banking, finance or similar business, or a corporation whose principal business is trading in securities for its own account.[121]) The latter of these two types of cases is not likely to be very significant, since it will be inapplicable if the foreign corporation has its principle office outside the United States, or if more than 50 percent of its stock is owned beneficially by five or fewer persons and their families.[122])

This provision will have its greatest impact in the case of a bank or loan company making loans to borrowers in foreign countries, which are arranged by an office in the United States. Although the various restrictions described in the case of income from rents and royalties are applicable here, the Committee Reports indicate that, in general, income will be allocated on an all or nothing basis—either all the income from a transaction will be allocated to the United States, or none will be.[123]) This is a surprising and forbidding conclusion, since it indicates that any significant participation by a United States office in the negotiation of a loan or sale of securities will result in United States tax on the entire income from the transaction. So far as can be learned from the Committee Reports, the fact that funds for a loan are provided from a foreign office would seem to have no influence on the amount of income subject to United States tax. Thus, quite surprisingly, the role of capital in such transactions would seem to be totally ignored.

118) Ibid.
119) I.R.C. § 864(c)(5)(B).
120) S. Rep. 21.
121) I.R.C. § 864(c)(4)(B)(ii). In general, income from foreign securities purchased solely for investment will not be affected by this provision. H.R. Rep. 65.
122) I.R.C. § 864(b)(2)(A)(ii). H.R. Rep. 65.
123) H.R. Rep. 65.

4. Sales of Personal Property

The last category of income from sources outside the United States of a foreign corporation subjected to United States tax by the FITA[124]) is income from sales of personal property, which is either inventory property or property held for sale to customers in the ordinary course of the taxpayer's business.[125])

Here again sales activity is the principal determinant of the extent to which income from sources outside the United States will be subject to tax in the United States. The limitations and restrictions discussed above in connection with income from leases and licenses of intangibles are also applicable here.[126])

Two other limitations come into play which are not applicable in connection with financial income or income from intangibles. First, if the property is sold for use or consumption outside the United States, and an office or fixed place of business of the foreign taxpayer outside the United States participates materially in the sale, no income from the sale will be taxed by the United States.[127])

The participation of an office abroad does not provide a basis for allocation of income, it provides a complete exclusion from United States tax. The foreign office will be considered to have participated materially in bringing about the sale if it solicited the sale, negotiated the contract, or performed significant services necessary to the consummation of the sale which were not subject to a separate agreement between the purchaser and seller.[128]) Thus, if the United States office of a French computer manufacturer arranges a sale of a computer to Canada, but the French office of the manufacturer performs installation and programming services necessary to the sale, and which were not separately contracted for, no United States tax would be imposed.[129]) The fact that a foreign office merely approves the contract or performs clerical functions in connection with the sale will not bring this exclusion into play.[130]) It is important to note that this exclusion is inapplicable if the personal property is sold for use, consumption or disposition in the United States.[131]) Thus, if the computer described in the previous example were sold F.O.B. Le Havre, for installation in the United States, the fact that employees of the French office of the corporation performed significant services in installing or programming the computer would not prevent the imposition of United States tax. Not all the income from the sale of the computer would be taxable in the United States. Since part of the income has its source in the manufacture of the computer and part in its sale, the income from the sale would be allocated on the basis of regulations long in force in the United States.[132])

124) See note 65, supra, with respect to certain income of insurance companies.
125) I.R.C. § 864(c)(4)(B)(iii).
126) I.R.C. § 864(c)(5).
127) I.R.C. § 864(c)(4)(B)(iii).
128) H.R. Rep. 67.
129) Section 864(c)(4)(B)(i) relating to rentals would also be inapplicable since it applies only to leases of intangibles.
130) H.R. Rep. 67.
131) I.R.C. § 864(c)(4)(B)(iii). See Reg. § 1.954-3(a)(3) as to when property is sold for use, disposition or consumption in a particular country.
132) Reg. § 1.863-3(b).

The second special limitation provides that with respect to property sold for use, consumption or disposition in a country other than the United States, taxable income shall not in any event exceed the income that would be taxed in the United States if the sale were made in the United States. In short, if the computer is delivered to a Canadian purchaser, and the sale is taxed in the United States (because the French office did not contribute significantly to the sale) the income taxed by the United States will not exceed that which would have been taxed if the computer had been delivered in the United States.[133])

5. Other Limitations

The Code contains two other limitations on the extent to which the United States will assert tax on foreign source income of a foreign corporation. Tax will not be imposed if the income constitutes "Subpart F" income—income taxable to the United States shareholders of the foreign corporation under the controlled foreign corporation provisions of the Code. The limitation is applicable even if the income is not actually so taxed to the foreign corporation's United States shareholders.[134]) And, dividends royalties and interest will not be taxed to a foreign corporation if it owns or is treated as owing stock having more than 50 percent of the voting power of the corporation paying these items of income.[135])

Some limitation upon these extensions of United States taxing jurisdiction will also be found in the various income tax conventions.[136]) However, the extent to which these limitations exist will vary from convention to convention.

6. The Foreign Tax Credit

Prior to the Act a foreign corporation, even though engaged in trade or business in the United States, was not allowed a credit for foreign income taxes paid.[137]) Such a credit was unnecessary since the United States did not tax foreign source income of foreign corporations, and the country of domicile of the corporation was expected to allow credit for any United States taxes paid on U.S. source income. However, under the Act certain foreign source income of a foreign corporation is subject to United States tax, and a real danger of double taxation exists. The income in question might be taxed by the country of its source, or might be taxed by the country of domicile with no credit allowed for the United States tax imposed. To prevent double taxation in either of these cases, section 906 of the Code allows a credit for foreign taxes paid with respect to income from sources without the United States which is taxed by the United States because it is "effectively connected."

133) I.R.C. § 863(b) and the regulations issued there under provide rules for allocating income having its source in more than one country.

134) I.R.C. §864(c)4(D)(ii).

135) I.R.C. § 864(c)4(D)(i).

136) See for example Reg. § 519. 107 (Canada) and Reg. § 505. 105(c), limiting the taxation of industrial and commercial crotits to income from sources within the United States.

137) I.R.C. (pre-FITA) §§ 901-904, 882(c)(3).

VI. OTHER SIGNIFICANT CHANGES CONCERNING THE TAXATION OF FOREIGN CORPORATIONS.

Two other changes made by the FITA deserve brief mention here.

Section 541 of the Code imposes a 70 percent tax on "personal holding corporations." Personal holding corporations are corporations more than fifty percent of whose stock is owned by five or fewer persons, and more than 60 percent of whose United States source "adjusted ordinary gross" income consists of personal holding company income—generally interest, dividends, rents, royalties and other types of investment income.[138]) The tax is applicable to foreign corporations,[139]) and cases of accidental subjection to the tax are probably not infrequent, although the tax is poorly enforced. Henceforth, a foreign corporation entirely owned directly or indirectly by foreign individuals not resident in the United States will generally be completely free of the tax.[140]) If less than ten percent of the corporation's stock is owned by U.S. citizens or residents, only a pro rata portion of the corporation's income will be subject to the tax.[141]) The tax will continue to apply, even in the case of a foreign corporation wholly owned by foreign individuals, if more than 60 percent of the corporation's United States source income (computed by excluding all income which would normally constitute personal holding company income) is from contracts which either require the personal services of a 25 percent shareholder of the corporation or under which the person to whom the services are rendered can designate the individuals who are to perform the services.[142])

Under the Act, as under prior law, dividends or interest paid by a foreign corporation may in some circumstances be deemed to be in whole or in part derived from sources within the United States and thus subject to 30 percent United States income tax.[143]) A number of the income tax conventions exempt dividends and interest paid by foreign corporations from this tax.[144]) If more than 50 percent of the worldwide gross income of the foreign corporation in the three year period[145]) ending with the taxable year preceding payment of the dividend or interest was effectively connected with the conduct of a trade or business in the United States, that portion of the dividend or interest which corresponds to the ratio between gross income effectively connected with local trade or business and worldwide gross income is considered paid from sources within the United States.[146]) This represents a considerable improvement over prior law.

138) I.R.C. §§ 542-544.
139) Reg. § 1.541-1(b); Rev. Rul. 60-34, 1960-1 C.B. 203.
140) I.R.C. § 542(c)(7).
141) I.R.C. § 545(a).
142) I.R.C. §§ 543(a)(7), B(1)(c), 545(d).
143) I.R.C. §§ 861(a)(1)(C), (a)(2)(B).
144) See, e.g., U.S.-Canada Income Tax Convention Art. XII.
145) Or for such period as the Corporation has been in existence.
146) I.R.C. §§ 861(a)(1)(C), (D); (a)(2)(B).

VII. CONCLUSIONS

Taken in their entirety, the provisions of the Foreign Investors Tax Act that we have discussed are hardly commendable for their simplicity. This failing is, however, in large part attributable to the awesome complexity of the Internal Revenue Code itself. That complexity is due in part to the tremendous complexity of the American economy; to the desire of both Governmental officials and taxpayers for specificity in the Code; to "loophole-plugging" efforts by the Treasury; and to exceptions written to meet special interests of groups of taxpayers, or even individual taxpayers.

The effort to eliminate the effects of the "force of attraction" principal has probably been a successful one, at least insofar as the great majority of cases are concerned. Cases arising in the fringe areas will continue to be a problem. However, where these problems are foreseen, the taxpayer has available to him the simple and generally effective tool of separate incorporation. Situations in which taxpayers stumble into these fringe areas will be the result of accident or lack of prior planning.

The venture into taxation of offshore income of foreign taxpayers seems ill-advised. It introduces substantial complexities into the Code, and relies at crucial points on vague terminology such as "material", "significant", "attributable" and "major." As a result, these provisions of the Code cannot be understood without resort to an extensive legislative history. Eventually they will have to be given more precise content by voluminous and complex regulations. It will probably be possible to avoid most of the effects of these provisions by changes in the mode of carrying on business. Taxpayers may generally be expected to make these changes whenever the impact of United States taxes would be significant, and many times these changes will adversely affect the United States balance of payments and result in reduced employment. Furthermore, it is unlikely that these new provisions in the Code will produce any significant increases in tax revenue. They are also undesirable because they make the problem of doing business in the United States more complex. This one area, aside, the Act would seem to have significantly improved the tax climate for investing and doing business in the United States.

* * * * DOCUMENTS * * * *

A SUMMARY OF THE INTERIM REPORT ON A LONG-TERM TAX SYSTEM IN JAPAN

The "Inquiry Commission for Tax System" continues to debate the structure of a long-term tax system, but has submitted an interim report to serve as a guide for tax reforms in 1967. As fiscal and economic conditions have changed markedly since the 1964 report was submitted, the commission has had to study the tax structure from a new angle.

This report is the tentative results of its study.*

PART I *Fundamental Approach*

Fiscal policy has recently passed through the development of the issuance of government bonds, and a new long-range economic plan has been made. At this opportunity, we must study our tax policy as a part of fiscal policy, and make a long-range plan for the tax system in order to maintain the stable growth rate of the economy.

1 *The tax burden and the allocation of resources between the public economy sector and the private economy sector*

To meet a changing society and economy, we must maintain a judicious distribution of the tax burden in order to secure a balanced allocation of resources between the public sector and the private sector. Although the public sector of the national economy will play an ever more important role in public finance, we must keep the tax burden at a level which fits the actual rise in national income lest we should improperly depress the level of activity in the private sector.

2 *Achievement of healthy family finance and the nurture of business*

In order to maintain the balanced development and expansion of the economy, it is necessary to stabilize national life as well as to improve the financial position of business enterprise. In planning our tax system we must always keep this point in mind.

(1) Family finances

We should take the following factors into consideration:

(i) The strong demand for a reduction in the individual tax burden;

(ii) The realization of equitable tax burdens between different types of income and different forms of business;

(iii) The re-distribution of income and wealth.

(2) Business

The stable growth of the economy is greatly affected by how business enterprises are

*) Reported by Hideyasu Iwasaki, Secretary General, Japan Tax Association.

taxed. We must investigate how enterprises should be taxed. In this connection, we should render more flexible what has been up to now a fairly uniform computation of taxable income and thereby encourage the internal retention of funds and cause the tax burden to fit the real condition of an enterprise.

3. *Counter-cyclical measures to maintain stable growth in the economy*

We should value highly the effect of a tax system itself in inducing business activity and countering a business cycle.

We should investigate not only how to counter a business cycle by raising and lowering the general tax rates, but also, on occasion, be ready to use tentative counter-cyclical measures.

PART II

1. *The level of the tax burden*

Since it is planned to increase the relative importance of the public sector of the economy in the future, inevitably as the income level rises the tax burden of the public will rise to a certain extent, but we should endeavor to continue to reduce the tax burden, particularly from individual income tax.

The level of the tax burden should strike a balance between family finance and business and consumption and saving in addition to a general level.

2. *A long-term tax system for family finance and business*

(1) Direct taxes

A. FAMILY (I.E.,) PERSONAL

A) Income tax

a. The taxable minimum

a) Personal exemption

It is desirable to set the minimum taxable income by taking the following factors into consideration.

(i) The fact that almost all high school graduates are now taxed;
(ii) The need for some spare income above the level of the cost of living;
(iii) The proportion of taxpayers to the employed population;
(iv) The number of persons at each income level;
(v) The level of income at which we can expect positive compliance by taxpayers in tax payment.

b) The system of personal exemptions

Under the present system of personal exemptions, Japan makes a distinction between the basic exemption, the spouse exemption and the dependency exemption, but it would be simpler and more desirable to fix a formal graduated scale for the amount deductible in accordance with an increase in the members of a household.

The deductions from tax (i.e. tax credit) for physically handicapped persons and

widows should be changed into exemptions from income to render the system uniform and more easily understood.

The deduction for life insurance premiums, the deduction for contributions, etc., the deduction for medical expenses and the deduction for miscellaneous losses should be combined into a single special deduction for expenditures permitting persons to do as they please up to a specified limit.

The remuneration income deduction should be raised in view of the peculiar character of remuneration income and the tax burden of unmarried persons.

The amount deductible from severance income should be raised as soon as possible up to the average level of the amount of severance income of those who leave work by the prescribed age.

The limitation on the amount deductible for persons employed by their own family (other than income from assets) (50,000 yen at present) should be raised only in view of the fact that a wife and children assist the father in earning his receipts and have less capacity to bear taxes.

b. The tax rates

The rate of progressivity in the tax rates should be ameliorated especially for income earners in the middle brackets, taking into consideration future increases in the level of income.

The present level of the minimum tax rate should be raised along with the adjustment in the minimum income taxable.

The maximum tax rate should be studied carefully from the standpoint of substantial equity in the tax burden and to maintain a balance with the maximum tax rate of the Inheritance Tax, since too high tax rates tend to induce income tax evasion and arbitrary distributions of assets and to discourage saving and investment.

Measures should be studied to offset, by means of a change in the tax rates, the tax reduction which high income earners would receive as a result of a raise in the minimum income taxable and a general reduction in tax rates.

c. The tax base

Aiming at the taxation of aggregate income as the ideal form of income taxation, we should investigate how to apply aggregate income taxation to interest income and dividend income, which are subject to separate taxation at present and to which the progressive rates are not applicable.

We should study the possibility of recognizing various accounting practices now prevailing among taxpayers in computing taxable income.

d. The taxable unit

Although there are those who hold that the taxable unit should be the family, when the present situation in Japan is taken into consideration, there exist many problems with regard to the adoption of the family as the taxable unit even in the case of employment income.

The present system of aggregating income from assets should be studied to discover

at what level the evil of dividing up the nominal titles to the assets will appear.

Aggregation of the income of spouses as the taxable unit would complicate the tax system and create the need for a basic revision in the tax rates. Therefore, it should be studied with great care.

B) The inheritance tax and the gift tax

These taxes play an important role in redistributing national wealth as taxes supplementary to the income tax.

a. The taxable minimum for the inheritance tax

Although the minimum amount taxable was raised twice this year, we should review the taxable minimum in accordance with the increase in individually-held property and the change in the national distribution of property from the standpoint of preserving the financial position of the family. In this respect the increase in the assessed valuation of a standard residence, in which persons of the middle class reside, should be taken into consideration.

b. The tax rates of the inheritance tax

In studying changes in the distribution of property, emphasis should be placed on fostering middle class property owners. Generally, inheritance tax rates should be connected up with the rates of the individual income tax, but when the taxable minimum is increased, from the standpoint of taxbearing capacity it ought not to be lower than the taxable minimum under the income tax.

c. The gift tax

The gift tax should be studied in connection with the inheritance tax as a tax supplementary to the latter to prevent abuses in the distribution of property before death.

d. Careful consideration should be given to effective and appropriate measures to increase corporate equity capital and to improve the financial structure of business entities, such as the flexible use and rationalization of the depreciation system for assets, in a way that will not conflict with the future basic structure planned for business enterprise.

B. BUSINESS

a. It is not desirable for the corporation tax—the basic tax on business—to tax only on an external basis and thereby tax businesses running at a loss. It should seek to tax business profits as a barometer of ability to pay tax.

b. The corporation tax system has been thought about too conceptually in the past. Rarely were the adjustment measures for dividends paid-out considered either from the payer's or the recipient's standpoint in terms of their conformity to actual dividends. Reduced tax rates apply to small and medium-sized corporations. Due to these facts, the trend of the tax system seems to have been in a direction whereby the corporation is to bear the corporation tax burden by itself. The present structure is a mixture of the

Shoup system and the F.R. German System (i.e., split and reduced tax rates for distributed income) and therefore its character is a bit ambiguous. In view of these circumstances, we should study how to put the corporation tax system into order so that it fits the present economy.

c. Based on the above approach, we should study the possible adoption of a profit tax under which the net profit of an enterprise will be regarded as an indicator of its taxable capacity as an entity apart from its shareholders. This change will involve many big problems, such as how to treat dividends and interest paid in computing net profit and how to deal with the present system which excludes dividends received from taxable income. Although such problems can probably be solved by careful consideration of the corporation tax rates, dividends from a subsidiary to its parent company and interim measures, etc., in order to avoid useless confusion, much time should be spent in studying the matter in the light of past experience until the tax system is understandable to at least the ordinary manager and investor.

(2) Indirect taxes

a. In regard to indirect taxes, etc., recognizing that the income elasticity of indirect taxes, etc., is different from that of direct taxes, efforts should be made in the direction of attaining an appropriate burden for indirect taxes, etc., by reducing them and giving priority to the income tax, so that the significance of indirect taxes, etc., in the tax system will be little changed for at least several years to come.

Attention should be given to the tendency for the burden of indirect taxes, etc., on household consumption to decrease gradually even without tax reduction, as the real income level of the household rises. An effort should be made to grasp the actual situation of shifting to consumers and the influence on business management of each consumption tax, as perfect shifting may be blocked because of excessive competition among businesses.

No sales tax should be adopted now because of the problems of shifting, its influence on the price level, its pressure on firms in an unfavorable competitive position, etc.

b. Specific duties and ad valorem taxes should be examined carefully as to their shifting, taking into account the increase in the income and price levels. Reforms are to be carried out in order to conform their burdens to reality.

c. The burdens of taxes for financing road improvements, such as the gasoline tax and the local road tax, etc., should be considered together with other sources of revenue and changes in the Road Improvement Plan.

3. *Economic policy and the nature of the long-term tax system*

(1) Counter-cyclical policy and the tax system

Our present tax system has a very considerable automatic stabilizing effect due to the high income elasticity of tax revenue. But countercyclical measures which require an

amendment of tax legislation might not be sufficiently speedy to be able to meet a change in the business cycle. Therefore, a flexible tax system should be adopted which provides rapid anti-cyclical measures.

Since it can be particularly expected in the case of the corporation tax that through its taxation of business profits, which reflect changes in the economic level, it will perform an important function as a cyclical regulator, a basis should be enacted in legislation providing in advance such measures as changes within specified limits for tax interest on delays in the payment of the corporation tax under certain conditions, suspension of special depreciation for rationalization machinery during periods when the economy is overheated and later enlargement of special depreciation in periods of recession, in addition to other changes made for cyclical reasons each year.

(2) Harmonizing the tax system with economic policy—
special tax measures

The incentive aspects of the tax system should be appreciated and flexible measures should be taken in harmony with the purpose of various policies. However, the rationality of the purpose of each policy should be examined strictly and the tendency for special measures to become chronic vested rights should be met through their rapid abolishment.

DEVELOPMENTS IN INTERNATIONAL TAX LAW

CONVENTION ENTRE LE CANADA ET LE ROYAUME-UNI

L'honorable Mitchell Sharp, ministre des Finances, a annoncé le 12 décembre 1966 qu'une convention de portée très générale en matière d'impôt sur le revenu a été conclue entre le Canada et le Royaume-Uni.

La convention a été signée le 12 décembre 1966 par M. Sharp et le haut commissaire britannique, Son Excellence Sir Henry Lintott, K.C.M.G., à Ottawa.

La convention relative à l'impôt sur le revenu conclue en 1946 entre le Canada et le Royaume-Uni a pris fin en 1964. Elle a été remplacée en partie par une convention de portée restreinte, limitée à quatre catégories de revenu, qui a été signée en 1965. Des négociations subséquentes ont produit une convention de portée étendue, analogue aux conventions de même nature que le Canada a conclues avec d'autres pays. Les dispositions de la convention de 1965 sont incorporées à la nouvelle convention. Sous réserve d'approbation par les parlements canadien et britannique, les dispositions de la nouvelle convention entrent généralement en vigueur aux dates où la convention de 1946 a cessé d'être en vigueur, de sorte qu'il n'y a pas de solution de continuité entre les dispositions des deux conventions. Les dispositions de la nouvelle convention qui intéressent les nouveaux impôts britanniques sur les corporations et les gains en capital entrent en vigueur dès leur établissement.

La convention a pour objet principal d'éviter la double imposition du revenu que des personnes physiques et des personnes morales d'un des pays reçoivent de sources situées dans l'autre pays. Les impôts canadiens inclus dans le champ de la convention sont les impôts fédéraux sur le revenu, y compris l'impôt de sécurité de la vieillesse sur le revenu. Les impôts du Royaume-Uni qui sont inclus sont l'impôt sur le revenu y compris la surtaxe, l'impôt sur les bénéfices, l'impôt sur les corporations et l'impôt sur les gains en capital.

La convention vise à prévenir la double imposition surtout grâce à un régime de dégrèvements réciproques d'impôt selon lequel un des pays alloue sur l'impôt qui lui serait par ailleurs payable un dégrèvement jusqu'à concurrence de certaines limites à l'égard de l'impôt payé à l'autre pays, et aussi grâce à des règles prévoyant que, dans certains cas, le revenu pourra être imposé par un seul des pays.

Voici les principales dispositions de la convention:

1. *Dividendes.* Les deux pays conviennent de ne pas prélever d'impôt dépassant 15 p. 100 sur les dividendes versés par les sociétés résidentes d'un pays à des résidents de l'autre pays. Ainsi, le taux de retenue du Royaume-Uni, qui est normalement de 41¼ p. 100 sera réduit à 15 p. 100. Le changement s'applique à partir du 6 avil 1966, date d'entrée en vigueur du nouvel impôt de retenue britannique distinct. Comme les taux de l'impôt canadien de retenue s'appliquant aux non-résidents sont actuellement de 15 et 10 p. 100, ils ne seront pas diminués.
2. *Intérêt.* Les deux pays conviennent de ne pas prélever d'impôt dépassant 15 p. 100

sur l'intérêt payé, à partir de sources situées dans un pays, à des résidents de l'autre pays. Là encore le taux de retenue du Royaume-Uni, qui est normalement de 41¼ p. 100, sera réduit à 15 p. 100, cette fois à partir du 6 avril 1965. Les taux canadiens, qui sont actuellement de 15 p. 100 ou moins, ne seront pas diminués.

3. *Redevances à l'égard de brevets.* Les deux pays conviennent de ne pas prélever d'impôt dépassant 10 p. 100 sur les redevances à l'égard de brevets payées à partir de sources situées dans un pays à des résidents de l'autre pays. Le taux de retenue du Royaume-Uni passe de 41¼ p. 100 à 10 p. 100 à compter du 6 avril 1965 et le taux de l'impôt canadien de retenue est réduit de 15 p. 100 à 10 p. 100 à compter du 1er janvier 1965.

Voici d'autres caractéristiques marquantes de la convention:

4. *Incorporation des dispositions de la convention de 1965.*

Voici les plus importantes de ces dispositions:

a) la règle ordinaire de l'"établissement stable" selon laquelle les bénéfices d'une entreprise résidant dans un des deux pays ne sont pas imposables par l'autre pays à moins que l'entreprise n'ait un établissement stable (par exemple une succursale) dans cet autre pays, et seulement dans la mesure où les bénéfices sont attribuables à l'établissement stable; et

b) la règle voulant que le pays de résidence d'un particulier ou d'une entreprise ait seul le droit d'imposer les bénéfices qu'une entreprise tire de l'exploitation de navires ou d'aéronefs, les redevances de droits d'auteur d'un particulier ou d'une entreprise à l'égard d'une oeuvre littéraire, musicale ou artistique (films non compris); et les pensions et rentes (avec des exceptions protégeant la situation qui était faite à certains pensionnés en vertu de la convention de 1946).

5. *Surtaxe du Royaume-Uni.* La convention de 1946 accordait aux particuliers résidant au Canada une exonération de la surtaxe du Royaume-Uni sur le revenu provenant du Royaume-Uni autre que le revenu gagné. La convention proposée limite ou réduit à zéro l'impôt du Royaume-Uni sur les dividendes, intérêts, redevances de brevets et droits d'auteur, et pensions alimentaires; en somme, elle exempte de fait ces revenus de la surtaxe du Royaume-Uni.

6. *Pension alimentaire.* La pension alimentaire ou les paiements d'entretien doivent être exonérés d'impôt dans le pays d'où provient le paiement. Donc, l'impôt canadien de retenue qui s'applique aux non-résidents et est de 15 p. 100, ne sera pas prélevé sur des paiements de cette nature qui sont faits à des résidents du Royaume-Uni.

7. *Instituteurs et étudiants.* La convention prévoit que si un professeur ou instituteur qui est ou était résident de l'un des pays se rend dans l'autre pays pour une période ne dépassant pas deux ans, la rémunération qu'il reçoit pour enseigner est exonérée d'impôt dans cet autre pays. La convention porte également que si une personne se rend de l'un des pays à l'autre à titre de bénéficiaire d'une subvention, recue d'une source située dans le premier pays, au fins de recherches devant être conduites au cours d'une période ne dépassant pas deux ans, cette personne n'est pas imposée quant à la subvention par le pays où les recherches sont faites. Un étudiant ou un apprenti qui se rend de l'un des pays dans l'autre pour y poursuivre son instruction n'est pas imposé par le pays où il étudie quant aux remise qu'il reçoit de l'extérieur de ce pays pour son entretien.

8. *Employés en visite et personnes à leur propre compte.* La convention renferme la disposition habituelle voulant que, dans certaines circonstances, les employés, résidents d'un pays, qui séjournent dans l'autre pays, ne soient pas imposables par l'autre pays quant à la rémunération qu'ils reçoivent de leur employeur pour les services qu'ils rendent dans cet autre pays. La convention comporte aussi la règle qui figurait dans la convention de 1946 au sujet de la rémunération d'employés du gouvernement d'un pays qui rendent leurs services dans l'autre pays, savoir que leur rémunération n'est pas imposée par le gouvernement de cet autre pays, si ces employés résident à la seule fin d'y rendre lesdits services. Pareillement, un résident d'un pays qui exerce une profession libérale ou quelque autre activité indépendante de caractère analogue dans l'autre pays n'est assujetti à l'impôt dans cet autre pays que s'il dispose d'une base fixe dans ce dernier pays, mais seulement dans la mesure où son revenu est attribuable à cette base. Ces règles ne s'appliquent pas aux professionnels du spectacle ni aux athlètes qu'ils soient employés ou exercent à leur propre compte, lorsque ces artistes et athlètes peuvent être imposés par le pays qu'ils visitent quant au revenu qu'ils retirent de leur activité personnelle dans ce pays.

9. *Gains en capital.* La convention renferme sur l'imposition des gains en capital un article qui est sensiblement le même que l'article recommandé dans le modèle de convention en matière d'impôt sur le revenu de l'Organisation de coopération et de développement économique, organisation à laquelle le Canada et le Royaume-Uni appartiennent tous deux; cet article est aussi analogue presque en tous points à l'article correspondant de plusieurs des autres conventions conclues par le Canada en matière d'impôt, notamment la convention avec les Etats-Unis. Cette disposition permet que les gains provenant de l'aliénation de biens immobiliers soient imposés dans le pays où ces biens sont situés. Les gains provenant de l'aliénation de biens mobiliers qui font partie de l'actif d'un établissement stable peuvent être imposés dans le pays où l'établissement stable est situé. Les gains provenant de l'aliénation d'autres genres de biens, notamment, les biens mobiliers qui ne font pas partie de l'actif d'un établissement stable, ne sont imposables que dans le pays dont le cédant est résident.

10. *Cas spéciaux.* Outre l'engagement réciproque selon lequel le Royaume-Uni accorde un crédit à valoir sur son impôt au titre de l'impôt canadien prélevé sur le revenu provenant de sources canadiennes, le Royaume-Uni s'engage également à accorder un crédit à l'égard de l'impôt fondamental du Canada sur le revenu des sociétés lorsqu'une société résidant au Royaume-Uni touche un dividende d'une société résidant au Canada dont la première possède au moins 10 p. 100 des actions donnant droit de vote. Cette disposition ne restera en vigueur qu'aussi longtemps que le Canada continuera d'accorder une déduction dans le calcul du revenu imposable à l'égard des dividendes reçus des compagnies canadiennes de filiales au Royaume-Uni dont la compagnie-mère canadienne possède au moins 25 p. 100 des actions donnant droit de vote.

La convention porte que chaque pays exonérera les dividendes versés après le 5 avril 1966 par une compagnie qui est résidente à une personne résidant dans l'autre pays si certaines conditions sont remplies. Ces conditions sont que la compagnie qui verse le dividende tire au moins 90 p. 100 de son revenu d'une entreprise conduite par elle dans l'autre pays et que l'autre pays n'assujettisse pas cette entreprise à un impôt spécial sur les bénéfices des succursales.

La convention changera la méthode selon laquelle les compagnies canadiennes d'assurance-vie qui exercent leur activité au Royaume-Uni au moyen d'une succursale sont maintenant imposées par le Royaume-Uni en permettant à l'administration britannique de revenir à une formule utilisée en vertu de la convention de 1946 jusqu'au moment où cette formule fut prohibitée par une décision judiciaire en 1958.

11. *Impôts spéciaux sur les bénéfices des succursales.* La convention stipule qu'un impôt spécial prélevé sur les bénéfices des succursales gagnés dans un pays par un résident de l'autre pays ne doit pas dépasser 15 p. 100 (le taux canadien qui frappe actuellement ces bénéfices).

12. *Dispositions diverses.* La convention renferme des dispositions relatives à certains arrangements visant à éluder l'impôt, aux consultations en vue d'éviter la double imposition, à l'échange de renseignements et à l'extension de la convention à d'autres territoires.

13. *Date d'entrée en vigueur.* La convention n'entrera en vigueur que lorsqu'elle aura reçu l'approbation législative des deux pays. Il est probable que la date d'entrée en vigueur sera celle où la sanction royale sera donnée à la loi habilitante du Canada.

Communiqué Ministère des Finances, Canada.

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£100 PRIZE

The British Branch of the International Fiscal Assocation announces a Prize of £100 for an essay on the subject:

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3 Entries must be original works.
4 There is no age limit to entrants.
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6 Entries should not exceed 6,000 words.
7 Closing date for entries shall be 31st December, 1967.
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9 Entries, and enquiries, should be submitted to Mr. G.J. Bellenie, the Honorary Secretary, British Branch of the International Fiscal Association, 6, St. James's Square, London, S.W.1.

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volume 1 - Sections 1-47, including Regulations;
volume 2 - Sections 48-82 K, including Rating Act;
volume 3 - Sections 83-160 AO, including International Agreements Act;
volume 4 - Sections 161-266, including Taxation Administration Act. The index, issued separately as a handbook, is completely new and designed to facilitate the necessary research in tracing comparable decisions elsewhere in the legislation. The legislation is as of February 28, 1966 and includes all relevant decisions of the High Court and the Board of Review reported prior to this date. The editors of this publication, which are Australia's leading autorities on Income Taxation, are *F.C. Boch* and *E.F. Mannix*.

Library International Bureau of Fiscal Documentation, no. 41 E 15 - 41 E 19; 1769-1772, 1967

AUSTRIA

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We consider this to be a very useful commentary and are glad that a new loose-leaf commentary on this important tax has now been published.

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EDITORIAL:

TEN YEARS EEC

Ten years ago, on March 25, 1957, the treaty establishing the European Economic Community was signed. Its goal is the creation of an internal Common Market where entrepreneurs from each of the six Member States may compete with one another on an equal basis without being unduly hampered by discriminatory national legislation. This goal will be achieved in stages.

In the fiscal field, only a few provisions are made in the treaty. One of the most explicit provisions is Art. 99, according to which the EEC Commission had to fulfil the difficult job of considering in which way the interests of the Common Market, and the law of the various Member States concerning turnover taxes, excise duties and other forms of indirect taxation could be best harmonized. It had to submit proposals to the Council of Ministers which then had to act by means of unanimous vote!

Just before the second lustrum of the EEC treaty, on February 9, 1967, the six Members of the Common Market countries agreed to adopt the TVA—tax on value added—as a basis for turnover taxation, by accepting the two draft proposals of the EEC Commission. TVA will be effective in each State not later than January 1, 1970.

This important, big step is at the same time the first effective step towards the necessary tax harmonization. As to excise duties, studies were begun in 1965. A draft directive concerning harmonization of registration duties due at the creation of a corporation and of stamp duties has been published. As to direct taxes the treaty contains no special provisions, although national legislation must not have a distortive effect on the conditions of competition in the Market. So far, no recommendations have been made, although studies have been started.

In Art. 220 of the Treaty, it is stated that Member States shall as far as is necessary, engage in mutual negotiations with a view to ensuring, for the benefit of their nationals, the elimination of double taxation within the Community. Most EEC States, but not all of them, have bilateral conventions with one another.

The Standing Committee of Heads of Revenue Departments agreed in November 1966 that a multilateral convention would be a suitable means of regulating the avoidance of double taxation in the EEC.

There is no doubt however, that progress can only be made with the will of the partners. In this case one recalls the famous words of Sir Winston Churchill that if you say you cannot, you will not; if you say you will, you can.

It is this word "will", that is going to be the decisive factor in the "to be or not to be" of a fruitful EEC.

Dr. J. C. L. Huiskamp

* * * * ARTICLES * * * *

BOMCHIL PINHEIRO CLARO LAVALLE & BADO*:

CORPORATIONS AND TAXATION IN ARGENTINA

I. GENERAL COMMENTS

The structure of taxes in Argentina is fairly complex, and there are various taxes which affect corporations, even though most of them are not specifically intended to tax the corporate form of business enterprises.

The most important of these taxes are the following:

1. INCOME TAX

Affects all profits arising as a result of the taxpayer's engagement in business, industry, mining or farming enterprises or in any other form of activity implying the purchase, sale, exchange or other form of disposal of goods.

2. 1966 EMERGENCY TAX

This is a surtax calculated as a percentage on the income tax corresponding to the year 1966.

3. EVENTUAL GAINS TAX

Is imposed principally on capital gains arising out of the disposal of goods which do not normally constitute a merchandise for the taxpayer.

4. LUCRATIVE ACTIVITIES TAX

This is not a federal tax, but is imposed by the Municipality of the Federal Capital and by the provinces and municipalities therein, on all activities performed with the intention of realising a profit; the main characteristic of this tax is that it is calculated on gross income, and that a surcharge of 20% on the resulting tax is usually applicable to corporations.

5. SUBSTITUTE INHERITANCE TAX

This is a tax on capital, intended to replace the inheritance tax which would otherwise be payable by persons inheriting shares in a corporation.

6. SALES TAX

Applicable on the first sale of manufactured or imported goods.

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*) This study has been prepared under the direction of "Le Cabinet Juridique spécialisé en Droit Sud Américain à Paris, Bomchil Pinheiro Claro Lavalle & Bado".

7. INTERNAL REVENUE TAXES

Under this name are grouped several taxes on consumption of certain specific types of goods (tobacco, alcoholic beverages, etc.)

8. TAX ON TRANSFER OF SHARES

In replacement of the income and eventual gains taxes which might apply to the profits arising from the sales of shares, a special tax was established, amounting to 1% of the gross amount of the transfer, which is consequently exempted from the income and eventual gains taxes.

9. [I]NSPECTION DUTY ON CORPORATIONS

It is a duty intended to reimburse the expenses incurred by the department of the Administration charged with supervising the activities of corporations. It is based on the nominal issued capital and cannot exceed Argentine Pesos 40.000 per year.

10. OTHER TAXES

In addition to the taxes mentioned above, there are some other taxes, mostly applicable to certain types of goods or activities, which do not specifically apply to corporations.

II. ANALYSIS of the MOST IMPORTANT TAXES

We shall give below a more detailed commentary on the first seven taxes included in the above list.

1. INCOME TAX

a) *Source:* The Argentine law, with only a few exceptions, is guided by the principle of the source, i.e., it taxes profits of Argentine source and exempts those having their source elsewhere. Consequently, it taxes all profits and other benefits arising from monies, goods or immaterial rights located, placed or used in the economic sense in Argentina, regardless of the nationality, domicile or residence of the owner or other parties to the operations and the place where the contracts are executed.

b) *Object of taxations:* All profits as defined in paragraph I. 1 preceding.

c) *Argentine corporations and foreign corporations having a permanent establishment in Argentina:* The Argentine law makes no distinction between these two types of corporations; taxes are liquidated on the same technical bases for both.

Companies constituted abroad are deemed to be corporations, unless proof to the contrary is presented, and if they do not have a permanent establishment in Argentina, are subject to a tax of 38.36% on all profits of Argentine source, to be withheld by whomsoever pays or credits the income to the foreign corporation.

d) *Liquidation of the tax:* The amount of profits on which the tax should be paid is determined on the basis of the commercial result of operations, adjusted in the manner set forth in the income tax law.

The general rule is that in order to determine the taxable income, from the gross income should be deducted all expenses incurred with the purpose of obtaining, maintaining and protecting such income, the law allows, however, the deduction of other amounts, most of them in the nature of tax incentives. On the other hand, the income tax itself and the eventual gains tax are not deductible.

There are very precise rules in the law as to the manner of valuing stocks, determining deductions for wear and tear, etc.

All profits of foreign source can be deducted in order to arrive at the taxable profit, as well as fiscal year losses carried forward from previous years, up to a maximum of ten years.

e) *Rate of tax:* On the taxable income thus determined, Argentine corporations have to pay a tax amounting to 33%, and branches of foreign corporations, to 38.36%. (This is not a discrimination against foreign corporations, but merely compensates the fact that dividends of the foreign corporations or their local branches are not subject to any further tax).

f) *Tax on dividends:* Argentine corporations have to pay, whenever they distribute profits, an additional tax amounting to 8% of the amounts placed at the disposal of the shareholders. This payment, which is borne by the corporation, constitutes the final settlement of tax payable on the dividends by the shareholders, be these domiciled in the country or abroad.

2. 1966 EMERGENCY TAX

This tax is a temporary measure, applying only to the taxable income of 1966; it amounts to 15% of the income tax payable for this year.

3. EVENTUAL GAINS TAX

The principle of taxing only profits of Argentine source described for the income tax also applies to this tax; it applies to the profit mentioned in I, 2 and the rate is 10%, being the same for Argentine corporations and for branches of foreign companies.

4. LUCRATIVE ACTIVITIES TAX

As a consequence of the rules in the National Constitution governing the right to tax of the Federal Government and of the provinces, the gross income of individual merchants and corporations could be taxed by both authorities. Double taxation thus resulted, and to avoid this, a convention was signed between the Federal Capital and the provinces, establishing rules for splitting the gross income (common basis for these taxes) between the various authorities, which can then apply to the part corresponding to them whatever rate of tax they deem proper. The rate thus varies from province to province, but it is usally about 1% of the gross income, and in many provinces a surtax of 20% of the resulting tax is assessed if the taxpayer is a corporation.

5. SUBSTITUTE INHERITANCE TAX

This tax on capital is applicable both to Argentine corporations and to branches of foreign corporations, as well as to some other groups of taxpayers. The tax is calculated

on the net capital, which is defined by the tax law as the difference between assets and liabilities, both adjusted according to the income tax rules. From the assets, those permanently located abroad can also be deducted. From the capital thus determined, the amount of the income tax and the emergency tax 1966 payable for the same financial period are deducted, and on the net result a tax of 1.5% is paid.

6. SALES TAX

This tax must be paid on all sales of merchandises, fruits and crops and other produces but in such a way that no product is taxed more than once. The fact that the taxpayer be a corporation has no influence at all on the amount of tax to be paid. The law provides a series of exemptions, referring mostly to articles of prime necessity and to agricultural products, provided these have not been subjected to any industrial treatment. The general rate of this tax is 10%, but there is a small group of products subject to a tax of 13% and another group, of popular use, subject to a smaller rate of only 3%.

7. INTERNAL REVENUE TAXES

These taxes are not technically related to each other, but are grouped together by the law for historical reasons. These are taxes on the consumption of certain articles, and in some cases are very similar to the sales tax. Normally, articles subject to internal revenue taxes are not subject to sales tax, and in the few cases where they are not exempted from the latter, the amount paid for internal revenue taxes must be deducted from the total sales to obtain the amount on which the sales tax will be calculated.

Among the articles and services subject to these taxes we may mention tobacco (including cigars, cigarettes, etc.), alcohol, alcoholic drinks, lighters, insurance, etc., each having its special rules for the determination and payment of the tax. These are taxes generally applied on the particular articles or services, and, therefore, the fact that the taxpayer be a local or foreign corporation has no bearing at all.

I

Corporations	Incorporated in the country		Have to file a tax return; rate 33 %; art. 54 of the law.
	Incorporated abroad	A) Having a permanent establishment in the country	Have to file a tax return; rate 38.36 %; art. 54, last paragraph of the law.
		B) Not having a permanent establishment in the country	Whomsoever pays or credits income of any kind, excluding dividends, has to withhold 38.36 %; art. 55 of the law.

II

Dividends	In every case the corporation has to pay 8 % on the dividends distributed	Individuals: Do not have to include the dividends in their tax returns as income, but have to include the shares in their declaration of assets and liabilities; art. 1, point 6, of decree-law No. 11,452/62
		Corporations: Do not have to include the dividends in their tax returns and they have a tax credit; art. 1, point 7, of decree-law No 11,452/62

III

Tax credits (corporations incorporated in the country); art. 1, point 7, of decree-law 11,452/62	If return shows taxable profit: 8 % on	dividends collected / dividends paid	whichever the lower	
	If return shows tax loss:	if dividends collected are bigger than the loss: 8 %	on the difference / on the dividends distributed	whichever the lower
		if dividends collected are less than the loss: No credit		

IV

Debentures, bonds and other securities (excluding shares); General Resolution No 1030	Holders living in the country:	Not making their name known, 38.36 % withholding (income does not have to be included in the tax return; art. 46, 1st paragraph of the law)
		Making their name known, 8 % withholding (income has to be included in tax return; art. 46, 2nd paragraph of the law)
	Shareholders resident abroad:	Withholding 38.36 %; art. 46, 1st paragraph of the law.

NOTE: Simultaneously with the withholding of the income tax, the emergency tax 1965/66 (15 % on the amount of the income tax) must be withheld; General Resolution No 1013.

B — INCOME PAID ABROAD

	WITHHOLDING to be MADE					
	If tax is to be borne by creditor (as provided by the law)			If tax is to be borne by debtor (by agreement between the parties)		
	Income tax %	Emergency tax 1964/65 %	Total	Income tax %	Emergency tax 1964/65 %	Total
1) Dividends (from ordinary and preferred shares only)	no withholding					
2) Income from other securities	38,36	5,7540	44,1140	68,6397	10,2960	78,9357
3) Fees to members of the Board, managing committees or other bodies, meeting abroad	38,36	5,7540	44,1140	68,6397	10,2960	78,9357
4) Fees for advice rendered from abroad — by corporations	34,5240 (38,36 on 90 %)	5,1786	39,7026	57,2562	8,5884	65,8446
4) Fees for advice rendered from abroad — by individuals	basic and additional progressive tax on 90 % plus emergency tax					
5) Interests paid — to corporations	38,36	5,7540	44,1140	68,6397	10,2960	78,9357
5) Interests paid — to individuals	basic and additional progressive tax plus emergency tax					
6) Royalties — if the licensor incurs in research and development expenses — corporations	34,5240 (38,36 on 90 %)	5,1786	39,7026	57,2562	8,5884	65,8446
6) Royalties — if the licensor incurs in research and development expenses — individuals	basic and additional progressive tax on 90 % plus emergency tax					
6) Royalties — if licensor does not incur in such expenses — corporations	38,36	5,7540	44,1140	68,6397	10,3960	78,9357
6) Royalties — if licensor does not incur in such expenses — individuals	basic and additional progressive tax plus emergency tax					
7) Other income — corporations	38,36	5,7540	44,1140	68,6397		
7) Other income — individuals	basic and additional progressive tax plus emergency tax					

I. CLASS:
Income of the second class includes:
a) royalties (Art. 43, a of the law)
b) Income perceived in one or more payments for the { temporary / or / final } transfer of royalties (Art. 43, c of the law)

II. LEGAL DEFINITION:
For the purposes of this law, royalty is defined as all consideration received in { money or other goods } for the transfer of { 1) ownership / 2) utilization / 3) consumption / 4) rights } of goods { the amount of such consideration being determined in relation to a unit of } { production / sale / exploitation / etc. } { whichever be the name given to such consideration } (Art. 44 of the law)

III. SOURCE:
Is considered of Argentine source: all income produced by ..... rights { placed / or / used } in the Argentine Republic (R.-S.-sec. b)
such as ..... the royalties.

IV DEDUCTIONS ADMITTED:

a) *Of a general nature:*
Those receiving royalties can deduct up to 25 % of the income received as depreciation of the invested capital until its amount has been fully deducted.
The Income Tax Department can authorize the adoption of a different percentage if special circumstances render it advisable. (Art. 65, 1st. paragraph of the law)

b) *Goods not losing their value:*
If the goods transferred temporarily to a third party be of such a nature not to suffer loss or waste in their value, such as:
— rights
— marks
— and other intangible assets
the person receiving royalty is not entitled to deduction mentioned in art. 65 of the law. (Art. 76 of the Regulatory Decree)

c) *Research and development expenses:*

1) *Enterprises located abroad* incurring habitually in research and development expenses to acquire goods capable of producing royalties, can only deduct 10 % of the royalties received in compensation of such expenses.
(Art. 65 of the law)
These expenses are presumed to represent 10 % of the gross royalties, unless evidence to the contrary is presented by the taxpayer.
(Art. 76 of the Regulatory Decree)

2) *Enterprises located in the country:*
They determine the profit derived from this type of income by deducting all research and development expenses incurred in the same period of time to which the income for royalties refers.

D — EXEMPT INTEREST

Interest arising from { Securities / Bills / Debentures and similar liabilities } issued by { public or private enterprises or financial establishments } to finance { works or investments } { declared of national interest for the purposes of this exemption by the National Government }

Fixed dividends of redeemable preferred shares, whether issued in pesos or in foreign currency

This exemption will remain in force until total cancellation or redemption of the securities or shares. (Art. 19, p of the law)

Interest of: development loans granted by { foreign / official } entities with the limitations established by the regulations. (Art. 19, s of the law)

These loans are those made by foreign official entities with the intention of granting help in the { cultural / scientific / economic / and / demographic } development of the country { provided interest does not exceed 6% } { and the payment is made over a period longer than 5 years } (Art. 34 of the regulations)

E — INCOME TAX

Source of Income	*Gross Profit* —	*Deduction from gross profit* =	*Net income* —	*Allowances for fiscal incentives* =	*Taxable income*
Income arising from: — merchandizing — industrial activities — mining activities — farm and cattle exploitation — other activities involving trading through selling, purchasing, exchanging or otherwise habitually disposing of goods. Exemptions 1) Interest from money deposited in savings accounts 2) Income of foreign source 3) Income from bonds, etc., issued by national, provincial or municipal governments 4) Interest from securities, debentures, etc., issued by private entities declared of national interest by the national government 5) Result of the sale of shares and other securities 6) Dividend from shares	Net sales less cost of production or cost of purchase.	1) Expenses and other costs necessary for the business operation (expenses necessary for obtaining, maintaining or keeping income) 2) Interest paid to creditors and expenses arising from obtaining, renewing or paying these debts 3) Taxes and duties imposed on income-producing goods 4) Insurance premiums 5) Extraordinary losses arising from calamities such as fire, etc., insofar as not covered by insurance 6) Losses arising from crimes comitted against the goods utilized in the exploitation by employees insofar as not covered by insurance 7) Contributions and other payments towards pension funds, provided these are administered by national, provincial or municipal entities 8) Donations to the Nation, provinces, municipalities and to institutions of public good 9) Depreciation for use on wastage and losses through lack of use 10) Royalties 11) Constitution expenses 12) Substitute inheritance tax 13) Fees or salaries paid to members of the board, councils or other bodies acting abroad 14) Fees to the board of directors and syndics 15) Bonuses to staff 16) Expenses or contribution towards expenses in benefit of the staff for medical assistance, schooling and cultural assistance, subsidies to sporting clubs and, in general, all expenses benefitting staff 17) Fees, etc., paid for technical, financial or other advice received from abroad Non-deductible expenses 1) Interest on own capital 2) Income tax, eventual gains tax and emergency 1965/66 tax 3) Taxes on capital 4) Depreciation of goodwill, trademarks or other intangible assets	1) Investments in the formation of woods 2) Direct exploring expenses in mining enterprises 3) Amounts invested in buying shares of electrical and agricultural cooperatives, up to a maximum of $100,000 4) Half the amounts invested in permanent pastures and permanent trees 5) Steer breeding expenses Deductible provisions 1) For bad debts 2) For mathematical reserves, current risks and similar (insurance) 3) For indemnity for staff dismissal Losses from previous years up to 10 years	Rate 33 %— Argentine corporations plus 8 % on distributed dividends less dividends received from other corporations 38.36 % — Branches of foreign corporations Less: Tax withheld payments on account (tax advances) Net amount payable

F — SUBSTITUTE INHERITANCE TAX

Subject of taxation	*Assets*	— *Assets to be excluded*	= *Taxable assets*	— *Liabilities*	= *Capital*
Capital and Reserves (Assets less Liabilities)	Total according to the balance sheet less: 1) memorandum accounts 2) loss carried forward among the assets 3) amounts owed by shareholders, not fully paid	1) Investment in shares 2) Goods situated permanently abroad		1) Liabilities towards third parties 2) Inrealized profits Deductible: Only the proportion corresponding to the taxable assets over the total assets.	Less: 1) Fees for board of Directors and Sundics (See note) 2) Participation in profits and bonus to Staff 3) Income tax for the year 4) Emergency tax for the year Not deductible: Substitute inheritance tax Tax payable: 1,5 % on the remainder

NOTE: Branches of foreign corporations cannot deduct fees to the Board of Directors and Syndics.

MINISTERE DES FINANCES A BURUNDI:

LA FISCALITE DIRECTE AU BURUNDI*)

RESUME

I. IMPOTS SUR LES REVENUS
- A. Impôt sur les revenus locatifs
- B. Impôt mobilier
- C. Impôt professionnel

II. IMPOT REEL
- A. Impôt foncier
- B. Impôt sur les véhicules

III. CONTRIBUTION PERSONNELLE MINIMUM

IV. IMPOT SUR LE GROS BETAIL

I. IMPOTS SUR LES REVENUS

La loi du 21 septembre 1963 a porté réforme des impôts sur les revenus.

Cette réforme a eu pour but d'améliorer les bases du développement économique tout en assurant une meilleure stabilité financière.

Le régime des impôts sur les revenus au Burundi se caractérise par une grande simplicité, des taux modérés, une absence totale de discrimination, et témoigne un intérêt certain aux problèmes économiques.

Les textes consacrent l'isolement fiscal du Burundi, qui renonce à imposer les bénéfices et les revenus réalisés à l'étranger. Par contre, les pertes subies par les établissements étangers du redevable ne peuvent en aucun cas influencer les résultats des exploitations au Burundi.

Le Burundi a donc déjà pris toutes les mesures internes en vue d'éviter les doubles impositions.

Par ailleurs, aucune discrimination n'est faite quant aux taux des impôts professionnels et mobiliers entre les sociétés de droit national et les sociétés étrangères. Ces dernières doivent simplement tenir une comptabilité spéciale des opérations traitées par leurs établissements au Burundi.

*) Cette étude (du 1er octobre 1966) a été redigée par le Ministère des Finances à Burundi et cordialement mise à notre disposition par M. Bonus KAMWENUBUSA, Directeur Général des Impôts et des Douanes.

Des exemptions d'impôt peuvent être accordées en vertu des dispositions du Code des Investissements, en vue d'accroître le mouvement des capitaux privés et de diriger ces capitaux dans le secteur des entreprises que le Burundi estime les plus productives et fondamentales pour sa croissance économique.

A. IMPOT SUR LES REVENUS LOCATIFS

Base

L'imposition à l'impôt sur les revenus locatifs est limitée aux revenus provenant d'immeubles situés dans le pays.

L'impôt est établi sur le revenu net.

Le revenu net est égal au revenu brut moins les charges, estimées forfaitairement à 20%.

Redevables

Sont redevables de l'impôt:

a) le propriétaire;

b) le sous-locataire

Taux

20% pour la première tranche de revenus de 200.000 fr;
25% pour la tranche de 200.001 à 400.000 fr;
30% pour la tranche de 400.001 à 600.000 fr;
35% pour la tranche de 600.001 à 800.000 fr;
40% pour le surplus.

Cet impôt s'applique aux revenus locatifs tant des sociétés que des personnes physiques.

B. IMPOT MOBILIER

Base

Revenus d'actions
d'obligations
de capitaux empruntés
de parts des associés non actifs
tantièmes aux administrateurs

Redevables

Sont tenues de payer l'impôt mobilier, les sociétés et les personnes qui paient les revenus mobiliers.

Fait générateur

Le paiement des revenus ou leur mise à la disposition du bénéficiaire.

Taux
20%

Remarque
Les revenus imposables à l'impôt mobilier dans le chef des sociétés étrangères sont déterminés forfaitairement à 50% de la base imposable à l'impôt professionnel. En d'autres termes, la détermination des dividendes et des intérêts payés à l'étranger mais ayant pour origine les bénéfices réalisés au Burundi se fait d'après une base forfaitaire. La combinaison des articles 14, 15 et 16 considère comme distribution 50% des revenus réalisés et imposés au Burundi, tant à l'impôt professionnel qu'à l'impôt sur les revenus locatifs.

C. IMPÔT PROFESSIONNEL

Base
Bénéfices (commerçants, industriels, agriculteurs);
Rémunérations;
Profits (professions libérales)

– Les revenus sont imposables sur leur montant net, c'est-à-dire en raison de leur montant brut diminué des dépenses professionnelles faites, pendant la période imposable, en vue d'acquérir et de conserver ces revenus.
– Les amortissements déductibles sont les amortissements nécessaires des biens servant à l'exercice de la profession, pour autant qu'ils correspondent à une dépréciation réellement survenue pendant la période imposable.
– Les revenus de l'année sont diminués des pertes professionnelles éprouvées pendant les trois années précédentes.
– Les impôts sur les revenus ne sont pas déductibles de la base imposable.
– Les accroissements résultant de plus-values réalisées ne sont imposables que dans la mesure où le prix de réalisation dépasse le prix d'acquisition, déduction faite du montant des amortissements déjà admis au point de vue fiscal.
– En vue d'éviter la double imposition d'un même revenu dans le chef d'un même redevable, les éléments déjà imposés au cours d'un exercice comptable sont déduits du montant des revenus imposables à l'impôt professionnel réalisés durant cet exercice, à concurrence de la partie nette des éléments déjà imposés qui se retrouve dans les dits revenus imposables à l'impôt professionnel (Article 59, § 1er).
– Est considéré comme résidant effectivement au Burundi:
a) celui qui, quelle que soit sa nationalité, a établi dans le Royaume son habitation réelle, effective, continue;
b) celui qui a dans le Royaume son domus, sa famille, son centre d'activité, le siège de ses affaires et de ses occupations;
c) celui qui a établi dans le pays le siège de sa fortune (Article 62).
– Les revenus professionnels des époux sont cumulés.
– Les sociétés étrangères qui exercent une activité au Burundi sont imposables sur les bénéfices réalisés par leurs établissements permanents ou leurs établissements fixes qui y sont situés.

– La réforme fiscale, en ce qui concerne les sociétés étrangères, a accepté le principe de la territorialité de l'impôt et de l'égalité complète entre les sociétés de droit national et les sociétés étrangères. Il n'y a donc aucune discrimination d'après la situation du siège social ou du principal établissement administratif. Toutes les sociétés, qu'elles soient étrangères ou de droit national, du moment qu'elles réalisent le même montant de bénéfices, supportent la même charge fiscale.
– L'article 69 a accepté le principe de l'existence d'un établissement permanent ou fixe dans le pays comme une condition nécessaire pour l'imposition au Burundi. La définition de l'établissement permanent ou fixe est celle adoptée par les conventions internationales en vue d'éviter la double imposition.
– Les bénéfices réalisés à l'étranger par une société nationale ou par une société étrangère ayant son activité principale au Burundi, ne sont pas imposables au Burundi.

Taux

– Les bénéfices des sociétés sont, pour le calcul de l'impôt, divisés en deux tranches. La première tranche est de 1.000.000 francs et la deuxième représente le surplus du bénéfice. Les taux de l'impôt sont fixés respectivement à 30% pour la première et à 40% pour la seconde tranche. (Article 83).
– Pour les personnes physiques l'impôt est fixé à 5% pour la première tranche de revenus de 30.000 francs;

8% pour la tranche de 30.001 à 100.000 francs;
12% pour la tranche de 100.001 à 200.000 francs;
15% pour la tranche de 200.001 à 300.000 francs;
19% pour la tranche de 300.001 à 400.000 francs;
23% pour la tranche de 400.001 à 500.000 francs;
27% pour la tranche de 500.001 à 600.000 francs;
31% pour la tranche de 600.001 à 700.000 francs;
34% pour la tranche de 700.001 à 800.000 francs;
36% pour la tranche de 800.001 à 900.000 francs;
38% pour la tranche de 900.001 à 1.000.000 francs;
40% pour le surplus. (Article 84).

– La cotisation des contribuables établie par application de l'article 84 est réduite d'une quotité de 5% pour chacun des quatre premiers membres de la famille à charge (Article 89, 1er alinéa).
– Est déduite de la cotisation due, la contribution personnelle minimum acquittée pour le même exercice.
– La déclaration des personnes physiques doit être remise avant le 1er avril ou dans les 3 mois de la clôture de l'exercice comptable (Article 98, 1er alinéa).
– La déclaration des sociétés doit être remise au plus tard six mois après la clôture de l'exercice comptable (Article 99, 1er alinéa).
– Les impôts enrôlés, à l'exception de ceux dûs au moment de la vérification de la déclaration ou par retenue ou encore immédiatement exigibles, doivent être payés intégralement entre les mains du Receveur des Impôts, au plus tard le dernier jour du deuxième mois qui suit celui de l'envoi de l'avertissement-extrait du rôle (Article 122).

– L'impôt mobilier et l'impôt professionnel perçus par retenue sont payables entre les mains du Receveur des Impôts dans les quinze jours qui suivent le trimestre pendant lequel les revenus ont été payés ou mis à la disposition du bénéficiaire (Article 123, 2e alinéa).
– Les sociétés étrangères, de mêmes que les redevables qui, sans avoir au Burundi leur domicile ou leur résidence, y possèdent un ou plusieurs établissements quelconques doivent avoir un représentant au Burundi qui est tenu solidairement avec eux au paiement des impôts, et des accessoires (Article 137, § 1er).
– Sous peine de déchéance, la réclamation doit être présentée au plus tard dans un délai de six mois à partir de la date de l'avertissement-extrait du rôle ou de celle du paiement pour les impôts qui ne sont pas perçus par rôle (Article 139, § 3).
– Les impôts sur les revenus ne peuvent faire l'objet de taxes fiscales au profit des pouvoirs subordonnés, ni de centimes additionnels au profit des dits pouvoirs. Ces pouvoirs ne peuvent instaurer des taxes sur les revenus frappés par les impôts visés par la présente loi (Article 151).

II. IMPOT REEL
(loi du 17 février 1964)

A. IMPOT FONCIER

Base
La superficie des propriétés foncières bâties et non bâties situées au Burundi.

– Des exonérations de l'impôt foncier peuvent être accordées en vertu des dispositions du Code des Investissements (Article 5).

Redevable
– L'impôt foncier est dû par le propriétaire (Article 8).
– En cas de mutation d'une propriété, par suite de vente ou de toute autre cause, le nouveau propriétaire est tenu d'en faire la déclaration, au Département des Impôts, dans un délai d'un mois prenant cours à la date de ladite mutation. A défaut, le nouveau propriétaire est tenu au paiement de tous les impôts fonciers restant dus, relatifs à l'immeuble, solidairement avec l'ancien propriétaire (Article 11, § 1er).

Taux
– L'impôt foncier sur la superficie des bâtiments et constructions est calculé aux taux ci-après, par mètre carré de superficie:
30 francs à Bujumbura;
20 francs à Gitega;
10 francs ailleurs (Article 13).
– Le taux est fixé à un franc par mètre carré de superficie non bâtie (uniquement à Bujumbura) (Art. 19).

– *Période imposable et débition de l'impôt*

L'impôt foncier est dû pour l'année entière sur la superficie imposable existant au 1er janvier de l'année qui donne son nom à l'exercice fiscal sans que la mutation de propriété dans le cours de la dite année puisse donner lieu à dégrèvement (Article 21).

– La déclaration doit être remise avant le 1er avril de l'année de l'exercice pour les éléments dont le redevable est propriétaire au 1er janvier (Article 35).

– Sauf notification contraire du contribuable avant le 1er janvier de l'année de l'exercice, les plus récentes déclarations sont valables pour les années suivantes.

B. IMPOT SUR LES VÉHICULES

Base

Les véhicules utilisés sur route au transport de personnes, de marchandises ou d'objets quelconques.

Taux.

L'impôt est calculé par véhicule selon les cas, ou selon la puissance du moteur ou le poids.

Le taux de l'impôt sur les véhicules est fixé comme suit:

A. Cycles et cyclomoteurs d'une cylindrée ne dépassant pas 50 cm^3: 100 francs par véhicule.
B. Motocyclette, tricycles et quadricycles à moteur: 900 francs par véhicule;
C. Véhicules automobiles dont le poids n'excède pas 2.500 kgs: 300 francs par cheval-vapeur;
D. Véhicules automobiles dont le poids excède 2.500 kgs, ainsi que remorques et semi-remorques: 240 francs par 100 kgs de poids;
E. Véhicules tracteurs: sont imposables, selon le cas, au taux prévu sous C ou D ci-dessus.

Période imposable et débition de l'impôt

L'impôt sur les véhicules à moteur est dû pour l'année entière s'ils sont utilisés au cours du mois de janvier. Il n'est dû que pour un douzième par mois ou fraction de mois si l'usage commence après le mois de janvier (Article 43, 2e alinéa).

– En cas de cessation d'usage dans le courant de l'année d'un véhicule à moteur, le contribuable a droit au dégrèvement de la partie de l'impôt correspondant à la période qui suit le mois au cours duquel a eu lieu cette cessation d'usage (Article 44).

– Sauf notification contraire du contribuable avant le 1er janvier de l'année de l'exercice, les plus récentes déclarations sont valables pour les années suivantes (Article 51).

– Celui qui vend ou qui cède un véhicule imposable ou qui le met temporairement ou définitivement hors d'usage, doit en faire la déclaration dans la quinzaine au Receveur des Impôts (Article 52).

– Aussi longtemps que la vente ou la cession d'un véhicule à moteur n'a pas été déclarée, l'ancien détenteur est responsable de l'impôt, sauf son recours contre l'acquéreur (Article 54).
– Les impôts établis par la présente loi ne peuvent faire l'objet d'attribution ni d'impôts similaires au profit des pouvoirs subordonnés, ni de centimes additionnels au profit desdits pouvoirs.

III. CONTRIBUTION PERSONNELLE MINIMUM

Redevables
Les personnes physiques adultes qui résident effectivement au Burundi.

Taux
Chiffre variant de 400 à 1.500 francs en fonction des revenus ou des ressources.

Lieu d'imposition
Le contribuable paie la contribution personnelle minimum de la commune et à la commune dans laquelle il réside effectivement.

Réclamations
Les réclamations relatives à la redevabilité, l'exigibilité et à la perception sont adressées au Bourgmestre.
Pour être recevable, la réclamation doit être motivée. Sous peine de déchéance, la réclamation doit être présentée au plus tard dans un délai de six mois à partir de la date du paiement.
Il est délivré reçu de la réclamation.

Attributions
Le Ministre des Finances propose annuellement au Parlement les quotités de l'impôt qui seront attribuées au Pays d'une part, aux communes d'autre part (Article 32).
La contribution personnelle minimum ne peut faire l'objet de taxes fiscales communales, ni de centimes additionnels au profit des communes (Article 33).

IV. IMPOT SUR LE GROS BETAIL

Redevable
L'impôt est dû par le détenteur du bétail à partir du 1er janvier de l'année de l'exercice (Article 2).

Taux
Le taux de l'impôt est fixé à 120 francs par tête de gros bétail. Il sera revu annuellement et pourra être modifié suivant proposition du Ministre des Finances (Article 4).

Lieu d'imposition

Le détenteur de gros bétail paye l'impôt à la commune dans laquelle se trouvent les éléments imposables (Article 6).

Réclamations

Les réclamations relatives à la redevabilité, l'exigibilité et à la perception sont adressées verbalement ou par écrit au Bourgmestre de la commune où se trouvent les éléments litigieux.

Pour être recevable, la réclamation doit être motivée.

Sous peine de déchéance, la réclamation doit être présentée au plus tard dans un délai de six mois à partir de la date du paiement.

Il est délivré reçu de la réclamation (Article 17).

Attributions

Le Ministre des Finances propose au Parlement les quotités de l'impôt qui seront attribuées annuellement au Pays d'une part, aux communes d'autre part.

* * * * DOCUMENTS * * * *

WARUM IST DIE DEUTSCHE UMSATZSTEUER NICHT VERFASSUNGSWIDRIG?

Das Bundesverfassungsgericht hat am 20.12.1666 entschieden:
„Der Mangel an Wettbewerbsneutralität des geltenden Umsatzsteuergesetzes, soweit es sich um die „einstufigen" und „mehrstufigen" Unternehmen handelt, muss bis zum Abschluss der eingeleiteten und in angemessener Zeit vom Gesetzgeber zu verabschiedenden Umsatzsteuerreform hingenommen werden. Dasselbe gilt für die Organschaft".

Diese Entscheidung wird, unserer Meinung nach, die baldige Einführung der Netto-Umsatzsteuer zu einer Conditio sine qua non machen.

Wir publizieren nachstehend den vollständigen Text der auch von internationalem Gesichtspunkt aus interessanten Begründung des Gerichtshofes[1]).

Urteil des Ersten Senats vom 20. Dezember 1966 — 1 BvR 320/57, 1 BvR 70/63 — in dem Verfahren über die verbundenen Verfassungsbeschwerden.

I. der Firmen
1. — 42. . . .
gegen die Regelung der Organschaft durch Artikel 2 des Neunten Gesetzes zur Änderung des Umsatzsteuergesetzes vom 18. Oktober 1957 (Bundesgesetzbl. I S. 1743) in Verbindung mit Artikel 1 Ziffer 1 des Elften Gesetzes zur Änderung des Umsatzsteuergesetzes vom 16. August 1961 (Bundesgesetzbl. I S. 1330),
bei der Beschwerdeführerin zu 1 auch gegen die Einspruchsentscheidung des Finanzamts . . . vom 18. November 1957 — StNr. 23/27 —;

II. der Firma . . .
gegen des Urteil des Bundesfinanzhofs vom 13. Dezember 1962 — V 87/60 S —[2]).

ENTSCHEIDUNGFORMEL:

Die Verfassungsbeschwerden werden zurückgewiesen.

GRÜNDE:

A.
I.

1. Die deutsche Umsatzsteuer hat ihren Ursprung in der Finanznot des ersten Weltkrieges: Das Gesetz über einen Warenumsatzstempel vom 26. Juni 1916 führte eine Abgabe von 0.1% zunächst nur von allen Lieferungen eines gewerblichen Betriebes ein; das Umsatzsteuergesetz vom 26. Juli 1918 dehnte die Steuerpflicht auf alle Lieferungen und Leistungen aus.

In der folgenden Zeit wurde nicht nur der Steuersatz erheblich erhöht, sondern auch der Umsatzsteuerrecht selbst weiter ausgestaltet. Erneut kodifiziert wurde es durch das Umsatzsteuergesetz vom 16.

1) Bundessteuerblatt 1967, Teil III, Nr. 1, S. 7 ff.
2) BStBl 1963 III S. 72

Oktober 1934 (RGBl. I S. 942). Nach zahlreichen Änderungen hat der Bundesminister der Finanzen am 1. September 1951 eine Neufassung bekanntgemacht (BGBI. I S. 791) — UStG —. In dieser Fassung gilt das Gesetz noch heute; in Einzelheiten ist es mehrfach geändert worden.

Das Bundesverfassungsgericht hat durch die Entscheidung vom 5. März 1958 (BVerfGE 7, 282) den seit 1934 geltenden § 8 für nichtig erklärt. Er lautete:

„Zusatzbesteuerung für mehrstufige Unternehmen

§ 8

Der Reichsminister der Finanzen wird ermächtigt, Maßnahmen zum Ausgleich der verschiedenen Umsatzsteuerbelastung der einstufigen und der mehrstufigen Unternehmen zu treffen."

Das Aufkommen der Umsatzsteuer fließt dem Bunde zu (Art. 106 Abs. 1 Nr. 3 GG); es betrug im Rechnungsjahre 1965 brutto rund 24 Milliarden DM und damit etwa 41% der Steuereinnahmen des Bundes. Dem Bund steht die konkurrierende Gesetzgebung über die Umsatzsteuer sowie ihre Verwaltung zu (Art. 105 Abs. 2 Nr. 1, Art. 108 Abs. 1 GG).

2. Den allgemeinen Steuergegenstand bestimmt § 1 Nr. 1 UStG wie folgt:

„Der Umsatzsteuer unterliegen die folgenden Umsätze:

1. die Lieferungen und sonstigen Leistungen, die ein Unternehmer im Inland gegen Entgelt im Rahmen seines Unternehmens ausführt . . .
2. . . .
3. . . ."

Unternehmer in diesem Sinne ist, „wer eine gewerbliche oder berufliche Tätigkeit selbständig ausübt" (§ 2 Abs. 1 Satz 1). Sein Unternehmen kann aus mehreren Betrieben bestehen, auch wenn die Betriebe ganz verschiedenartig sind. „Das Unternehmen umfaßt die gesamte gewerbliche oder berufliche Tätigkeit des Unternehmers" (§ 2 Abs. 1 Satz 2).

Der Begriff der Lieferung ist in § 3 des Gesetzes dahin definiert: „Lieferungen sind Leistungen, durch die der Unternehmer den Abnehmer . . . befähigt, im eigenen Namen über einen Gegenstand zu verfügen".

Der Unternehmer vollbringt die Lieferung, indem er den Gegenstand an einen Abnehmer, also an eine andere Person weitergibt. Eine solche Lieferung wird — unter dem Aspekt des Weges der Ware vom Erzeuger zum Verbraucher — häufig als „Phase" oder als „Stufe" bezeichnet. Da das Entscheidende die Übertragung der Verfügungsgewalt an eine andere Person ist, wird diese Lieferung von Rechtsprechung und Rechtslehre als „Außenlieferung" oder „Außenumsatz" gekennzeichnet.

Damit scheiden als steuerpflichtig solche lieferungsartigen Vorgänge aus, bei denen ein Gegenstand innerhalb desselben Unternehmens von einem Betrieb an einen anderen oder von einer Betriebsabteilung an eine andere weitergegeben wird, also in der wirtschaftlichen Verfügungsgewalt desselben Unternehmers verbleibt. Diese Vorgänge werden allgemein als „Innenlieferungen" bezeichnet.

Besteuerungsmaßstab ist das von dem leistenden Unternehmen vereinnahmte Entgelt (§ 5). Der Steuersatz, der ursprünglich 0,1% des Entgelts betragen hatte, wurde mehrfach geändert. Vom 1. Januar 1932 ab betrug er allgemein 2%, vom

1. Januar 1946 ab 3%. Seit dem 1. Juli 1951 gilt ein allgemeiner Satz von 4% (§ 7 Abs. 1 UStG).

Aus wirtschafts- und sozialpolitischen Gründen sind gewisse Umsätze steuerfrei (§ 4) — so allgemein die Ausfuhr oder die Lieferungen landwirtschaftlicher Produkte und mancher Lebensmittel — oder mit einem geringeren Satz zu versteuern (§ 7 Abs. 2 bis § 7 c); so beträgt der Steuersatz für bestimmte Lieferungen im Großhandel nur 1% (§ 7 Abs. 3, §§ 7 b und 7 c). Unternehmer mit einem jährlichen Gesamtumsatz bis 120 000 DM genießen Ermäßigungen (§ 7 a).

Steuerschuldner ist der liefernde Unternehmer (§ 9). Das UStG setzt stillschweigend voraus, daß er den von ihm zu zahlenden Steuerbetrag im Preise an seinen Abnehmer abwälzt. Es verbietet aber grundsätzlich, die Steuer neben dem Entgelt gesondert anzufordern (§ 10).

3. Die nach diesem System erhobene Umsatzsteuer wird als eine „kumulative Allphasenbruttoumsatzsteuer" bezeichnet. Steuerpflichtig sind nicht nur eine einzige oder einzelne Umsatzphasen — wie etwa die Lieferung nur des Herstellers (Herstellerumsatzsteuer) oder nur des Einzelhändlers (Kleinhandelsumsatzsteuer) —, sondern alle Fälle (Phasen) der Lieferung eines Unternehmens an einen Abnehmer. Die Steuer wird von dem vollen Entgelt für die jeweilige Lieferung erhoben. Auch soweit das Entgelt den in früheren Phasen gezahlten Betrag an Umsatzsteuer enthält, ist es Besteuerungsmaßstab.

Die Beschränkung des Steuergegenstandes auf Außenlieferungen, das Entgelt als alleiniger Besteuerungsmaßstab sowie der feste Steuersatz (von allgemein 4%) sind die Faktoren, die den Steuerbetrag für den einzelnen Umsatz ergeben. Unabhängig ist seine Höhe von der jeweiligen Wertmehrung, die der Gegenstand in der Hand des liefernden Unternehmens erfahren hat, oder von der Höhe der Steuerbeträge, die die in der Umsatzkette vorausgehenden Unternehmen aufgewendet haben.

Ein Produkt wird, bevor es den Endabnehmer erreicht, regelmäßig eine mehr oder weniger lange Kette von Fertigungs- und Handelsstufen (Gliedern) durchlaufen. Unternehmen, die mehrere Glieder einer solchen Produktionskette in sich vereinen, werden allgemein als „mehrstufige", diejenigen, die nur ein Glied umfassen, allgemein als „einstufige" Unternehmen bezeichnet.

4. Der Begriff „umsatzsteuerliche Organschaft" — kurz: Organschaft — bezeichnet die umsatzsteuerlichen Wirkungen, die an den tatsächlichen Zustand der Beherrschung einer juristischen Person des privaten Rechts durch einen Unternehmer anknüpfen. Sie bestehen in folgendem: Lieferungen innerhalb des Organkreises, d. h. von dem herrschenden an die beherrschten Unternehmen und umgekehrt, sowie zwischen den beherrschten Unternehmen untereinander gelten als Innenlieferungen und sind daher umsatzsteuerfrei. Schuldner der Umsatzsteuer ist nur das herrschende Unternehmen, und zwar sowohl für die eigenen Außenlieferungen als auch für die der „Töchter" an außerhalb des Organkreises stehende Abnehmer. Dabei kommt es auf die Rechtsform des beherrschenden Unternehmens nicht an; es kann eine natürliche Person, eine Personengesellschaft jeder Rechtsform oder eine juristische Person sein; beherrschtes Unternehmen kann dagegen nur eine juristische Person des privaten Rechts sein. § 2 Abs. 2 Nr. 2 UStG definiert die Organschaft folgendermaßen:

„Die gewerbliche oder berufliche Tätigkeit wird nicht selbständig ausgeübt,

1. . . .
2. wenn eine juristische Person dem Willen eines Unternehmers derart untergeordnet ist, daß sie keinen eigenen Willen hat . . ."

Diese Organschaft ist erstmalig im Umsatzsteuergesetz vom 16. Oktober 1934 geregelt worden. Nachdem sie durch eine Maßnahme des Kontrollrats ab 1. Januar 1946 im wesentlichen außer Kraft gesetzt war, ist sie durch das Neunte Gesetz zur Änderung des Umsatzsteuergesetzes vom 18. Oktober 1957 (BGBl. I S. 1743) wiederhergestellt worden. Das Gesetz vom 16. August 1961 (BGBl. I S. 1330) hat ihre Voraussetzungen erschwert.

II.

Die Beschwerdeführerinnen machen geltend, das System der Allphasenbruttoumsatzsteuer sowie die Organschaft benachteiligten sie im Wettbewerb gegenüber den mehrstufigen Unternehmen, bedrohten ihre Existenz und seien daher verfassungswidrig.

1. Die Beschwerdeführerinnen zu I sind kleinere und mittlere „einstufige" Unternehmen vor allem der metallbearbeitenden und -verarbeitenden, teilweise auch der kunststoffverarbeitenden Industrie, der Herstellung von elektrotechnischen Materialien und Artikeln anderer Produktionsbereiche. Sie wenden sich unmittelbar gegen die Wiedereinführung der Organschaft durch § 2 Abs. 2 Nr. 2 UStG in der Fassung des Gesetzes vom 18. Oktober 1957, und zwar auch in der beschränkten Form des Gesetzes vom 16. August 1961; sie bitten, die Organschaft für nichtig zu erklären.

Die Beschwerdeführerin zu I 1 ficht mit ihrer Verfassungsbeschwerde außerdem ihren Umsatzsteuerbescheid für das Jahr 1956 und den Einspruchsbescheid an.

Die Beschwerdeführerin zu II liefert und montiert elektrische Anlagen; diese bezieht sie von der Elektroindustrie. Wegen des Umsatzes solcher Anlagen ist sie durch zwei Bescheide für die Jahre 1951 bis 1956 zu einer Umsatzsteuer in Höhe von rund 53 000 DM veranlagt worden. Hiergegen hat sie den Rechtsweg bis zum Bundesfinanzhof erfolglos beschrifften.

Beide Beschwerdeführerinnen bitten, die gegen sie ergangenen Steuerbescheide und die diese bestätigenden gerichtlichen Entscheidungen als verfassungswidrig aufzuheben, soweit ihre Umsatzsteuerpflicht diejenige vergleichbarer mehrstufiger Unternehmen übersteigt.

2. Der Bundesfinanzhof hat in seinem gegen die Beschwerdeführerin zu II ergangenen Urteil (BStBl. 1963 III S. 72 = Slg. Bd. 76, 204) die Verfassungsmäßigkeit des geltenden Umsatzsteuersystems, insbesondere der geringeren Belastung der mehrstufigen Unternehmer, mit der folgenden Begründung bejaht:

Die Umsatzsteuer knüpfe nicht wie eine Personensteuer an die Person des Steuerpflichtigen, sondern an den Steuergegenstand der Lieferung oder Leistung an und besteuere den im Wirtschaftsleben stattfindenden Leistungsaustausch oder — anders ausgedrückt — die wirtschaftliche Kraft, die sich darin äußere, daß eine Ware oder Leistung noch Absatz finde. Gerade ein Umsatzsteuergesetz könne bei der Vielfalt der wirtschaftlichen Erscheinungsformen, die es zu erfassen habe, nicht auf jede Besonderheit Rücksicht nehmen, sondern müsse sich darauf beschränken, typische Vorgänge zu regeln.

Unter diesem Gesichtspunkt sei es sachlich gerechtfertigt, wenn das Umsatzsteuergesetz Ungleiches gleich behandele.

Die etwaige Mehrbelastung der einstufigen Unternehmen sei nicht bedeutend. Die auf Abwälzung angelegte Umsatzsteuer belaste letzten Endes den Verbraucher und wirke als allgemeine Verbrauchsabgabe. Da aber nur die in dem Leistungsaustausch liegende wirtschaftliche Kraft besteuert werde, könne sich das einstufige Unternehmen nicht dadurch benachteiligt fühlen, daß ein mehrstufiges wegen geringerer Selbstkosten billiger verkaufen könne. Das Unternehmen sei nicht belastet, wenn und soweit die Marktlage ihm gestatte, die Umsatzsteuer in voller Höhe zu überwälzen. Nicht nur völlig gleiche Waren stünden im Wettbewerb; der Verbraucher könne zwischen verschiedenen Waren wählen; der Preis sei dabei für den Kaufentschluß nur ein Faktor unter vielen.

Ferner sei ein mehrstufiger Betrieb einem einstufigen nicht gleichartig; seine Organisation sei eine andere; die Kosten für Organisation und Personal, für die Betriebsmittel, die Werbung, die Lagerhaltung seien höher, das Risiko sei in vieler Hinsicht größer. Die geringere Umsatzsteuerbelastung des mehrstufigen Unternehmens sei nur einer — und nicht der bedeutendste — von vielen Kostenfaktoren und biete daher oft keinen Ausgleich für die Nachteile der Mehrstufigkeit. Unter Umständen spiele sie auch bei einem Satz von 4% eine geradezu untergeordnete Rolle. Umgekehrt beruhten die geringeren Selbstkosten und Preise mehrstufiger Unternehmen nicht immer auf der Umsatzsteuerersparnis, sondern oft auch auf einem größeren Kapitaleinsatz und rationelleren Fabrikationsmethoden. Die Konzentration in der Wirtschaft sei kein Beweis für umsatzsteuerliche Vorteile der mehrstufigen Unternehmen, sondern finde eine genügende Erklärung in zahlreichen anderen Gründen.

Eine Anzahl Änderungen des UStG habe dem geltenden System die ihm infolge des hohen Steuersatzes anhaftenden Härten genommen und auch den mittelständischen und damit einstufigen Unternehmen Vorteile gewährt. Auch diese Unternehmen hätten sich in den letzten Jahren wirtschaftlich günstig entwickelt. Die Umsatzsteuer dürfe nicht isoliert, sondern müsse im Rahmen des gesamten Steuersystems betrachtet werden. So mindere der als Umsatzsteuer gezahlte Betrag andere Steuern, insbesondere die Einkommen- und Körperschaftsteuer.

Die Mehrbelastung der einstufigen Unternehmen mit Umsatzsteuer sei daher nicht wesentlich, Maßnahmen im Sinne des früheren § 8 UStG seien nicht geboten. Die Herstellung einer vollen Gleichheit sei schon wegen der Unklarheit der Begriffe „einstufige“ und „mehrstufige“ Unternehmen nicht möglich. Zudem würde auch ein anderes Umsatzsteuersystem nicht völlig wettbewerbsneutral sein, insbesondere nicht die Mehrwertsteuer.

Schließlich sei die Umsatzsteuer in Zeiten von Krisen oder von hohem Finanzbedarf die bestgeeignete Steuer, da sie anders als die Ertragsteuern dem Fiskus sichere Einnahmen eröffne. Der Grundgesetzgeber habe die Umsatzsteuer ausdrücklich anerkannt, obgleich er ihr System und ihre Wirkung gekannt habe; ihre Beibehaltung durch den Bundesgesetzgeber sei eine wirtschaftspolitische Entscheidung.

3. Die Verfassungsbeschwerden sind vornehmlich auf eine Verletzung des Art. 3 Abs. 1 GG, daneben auch der

Art. 2 Abs. 1 und Art. 12 GG sowie des Sozialstaatsprinzips gestützt. Sie greifen das System der kumulativen Allphasenumsatzsteuer nicht schlechthin an, sondern nur innerhalb dieses Systems die einseitige Bevorzugung der mehrstufigen vor den einstufigen Unternehmen.

Die geltende Umsatzsteuer sei auf Abwälzung hin angelegt. Nur um die Erhebung zu vereinfachen, sei dem liefernden Unternehmen die Steuerpflicht aufgebürdet, endgültiger Steuerträger solle der Endverbraucher sein.

Die Außenlieferungen seien ein rechtsförmiger Tatbestand. Die Verteidiger des geltenden Umsatzsteuergesetzes wie die Bundesregierung stellten einmal — für das System allgemein — auf diese Rechtsförmigkeit des Verkehrs, ein anderes Mal jedoch — zur Rechtfertigung der Organschaft — auf die wirtschaftliche Seite ab. Für den wirtschaftlichen Vorgang sei es gleichgültig, ob er in einer Rechtsform, insbesondere des Kaufvertrages und der Übereignung durch ein einstufiges Unternehmen an ein anderes einstufiges Unternehmen, oder innerhalb eines mehrstufigen Unternehmens von einer Produktionsstufe an die andere ohne Kaufvertrag und Eigentumsübertragung erfolge. Die Selbständigkeit der liefernden Unternehmen und die Zahlung eines Entgelts seien daher als Kriterien des Steuergegenstandes jedenfalls im Rahmen der Allphasenumsatzsteuer sachfremd. Die gegenwärtige Regelung diskriminiere die einstufigen Unternehmen gegenüber den mehrstufigen. Gleiche Sachverhalte, nämlich die gleichen wirtschaftlichen Leistungen durch mehrstufige und durch einstufige Unternehmen, würden willkürlich ungleich behandelt. Verfassungsrechtlich entscheidend sei dabei, daß der Staat diese Ungleichheiten geschaffen habe; sonstige, nicht von hoher Hand verursachte Ungleichheiten der Produktionsbedingungen der einzelnen Betriebe seien, was der Bundesfinanzhof in seiner rein wirtschaftlichen Betrachtungsweise übersehe, für die verfassungsrechtliche Frage der Gleichbehandlung durch den Staat unerheblich.

Die Verfassungsbeschwerden beträfen nur die industrielle Fertigung, nicht dagegen andere Wirtschaftszweige wie den Groß- und Einzelhandel oder die Land- oder Forstwirtschaft. Für diese Verfassungsbeschwerden seien das richtige Vergleichspaar weder der Außenumsatz und der Innenumsatz noch die einstufigen und die mehrstufigen Unternehmen, sondern allein die Erzeugungsketten für gleiche oder ähnliche Produkte, deren Steuerlast — trotz gleichen Steuersatzes — ungleich sei.

Die industrielle Fertigung zeichne sich vor anderen Wirtschaftszweigen durch eine weitgehende Arbeitsteilung aus. Das gleiche oder ähnliche (homogene) Produkt könne sowohl in einer längeren Produktionskette hergestellt werden, deren Glieder mehrere selbständige Unternehmen mit jeweils geringer „Produktionstiefe", aber einer weitgehenden Arbeitsteilung seien, als auch durch ein einziges oder wenige Unternehmen mit verhältnismäßig großer Produktionstiefe. Es sei kein Grund vorhanden, beide Herstellungsarten (Produktionsketten) mit verschieden hoher Umsatzsteuer zu belasten.

Charakteristisch hierfür sei die Wettbewerbslage der Beschwerdeführerin zu II. In dem Kaufpreis, den sie für die von ihr montierten Anlagen an die liefernde Elektroindustrie zahle, sei der von dieser aufzubringende 4%ige Umsatzsteuerbetrag enthalten; dadurch, daß die Beschwerdeführerin außer von dem Rech-

nungsbetrag für die Kosten der Montage auch noch von dem Rechnungsbetrag für die ihren Kunden gelieferten Anlagen 4% Umsatzsteuer zahlen müsse, werde die Anlage zweimal mit Umsatzsteuer belastet. Werden sie dagegen von der Elektroindustrie in Konkurrenz mit der Beschwerdeführerin montiert, so werde sie nur einmal, nämlich mit dem vom Abnehmer unmittelbar an das Elektroindustrieunternehmen gezahlten Entgelt, mit Umsatzsteuer belastet; dies gebe der Elektroindustrie einen Wettbewerbsvorsprung.

Das herrschende System verletze auch das „Grundrecht der Chancengleichheit". Das Gesetz über Wettbewerbsbeschränkungen versperre die frühere Möglichkeit, durch Vereinbarung der Unternehmen die ungleich Belastung mit Umsatzsteuer auszugleichen, und mache die Gleichheit im Wettbewerb zur Regel. Die Bevorzugung der mehrstufigen Unternehmen durch das Umsatzsteuergesetz sei ein Widerspruch innerhalb der Rechtsordnung. Sie fördere weiter die Konzentration in der Wirtschaft, behindere die freie Entfaltung der Persönlichkeit nach Art. 2 Abs. 1 sowie die freie Berufsausübung nach Art. 12 GG und widerspreche, da überwiegend die kleineren selbständigen Unternehmen benachteiligt würden, der Sozialstaatlichkeit.

Die §§ 2 und 3 UStG seien daher zwar nicht in vollem Umfange, aber jedenfalls teilweise nichtig; das ganze Umsatzsteuergesetz brauche nicht für nichtig erklärt zu werden.

Der frühere § 8 UStG zeige, daß das Gesetz unvollständig sei. Der Gesetzgeber hätte das überkommene Umsatzsteuersystem an den Gleichheitssatz des Art. 3 Abs. 1 GG durch ein Gesetz (nicht durch eine nichtige Ermächtigung zum Erlaß einer Rechtsverordnung) anpassen müssen.

Die Organschaft verschärfe die steuerliche Ungerechtigkeit. Etwa 3000 Organkreise kontrollierten 25% der Produktion. Die Organschaft nehme gerade den rechtsförmigen Verkehr von der Steuerpflicht aus und widerspreche daher dem zur Rechtfertigung des geltenden Systems herangezogenen Grundsatz, daß der Rechtsverkehr Steuergegenstand sei.

Die Ansicht der Bundesregierung, die Organschaft diene im Vergleich zu vollfusionierten Unternehmen wenigstens in gewissem Umfange einer selbständigen Willensbildung und Unternehmerinitiative in den beherrschten Gesellschaften, widerspreche dem klaren Wortlaut des Gesetzes, daß den Organgesellschaften nach ihrer Begriffsbestimmung der eigene Wille überhaupt fehle. Zwischen Einheitsunternehmen und aus Organgesellschaften zusammengesetzten Konzernen bestünden wesentliche Unterschiede, so in dem Umfang der Beteiligung und in der Haftung.

III

1. Die Bundesregierung hat ausgeführt: Die überkommene rechtliche Ausformung der Umsatzsteuer sei durch Art. 106 bis 108 GG und durch die bisherige Rechtsprechung des Bundesverfassungsgerichts bereits anerkannt.

Rechtstechnisch sei die Umsatzsteuer eine Verkehrsteuer, in ihrer wirtschaftlichen Zielsetzung eine Verbrauchsteuer. Auch nach dem Wegfall der Ausgleichsmöglichkeit gemäß § 8 UStG sei sie mit dem Grundgesetz vereinbar. Der Steuergegenstand sei für alle Unternehmen der gleiche. Nicht die wirtschaftliche, sondern die entgeltliche Leistung sei Gegenstand der Umsatzsteuer; sie falle an, wo wirtschaftliche Kraft zutage trete. Auch

wirtschaftlich unterscheide sich die Übertragung der Verfügungsgewalt an einen anderen unter Zahlung eines marktgerechten Entgeltes von der bloß tatsächlichen Übergabe eines verarbeiteten Gegenstandes innerhalb desselben Unternehmens ohne Entgelt; die technische Vergleichbarkeit sei unerheblich; die Innenlieferungen innerhalb eines Unternehmens seien daher Außenlieferungen nicht gleich. Die Umsatzsteuer belaste, da abwälzbar, die Unternehmen nicht. Die wirtschaftliche Konzentration werde durch zahlreiche andere Gründe als durch die Allphasenumsatzsteuer gefördert; jedenfalls dürfe der Gesetzgeber im Rahmen seiner Wirtschaftspolitik auch die konzentrierten Unternehmen begünstigen. Ihr etwaiger umsatzsteuerlicher Vorteil werde durch die Gewinnsteuern reduziert. Die Begriffe „mehrstufige" und „einstufige" Unternehmen seien seit der Nichtigerklärung des § 8 UStG keine gesetzlichen mehr; sie seien auch innerhalb eines Wirtschaftszweiges zu unbestimmt und praktisch nicht verwertbar.

Eine wirtschaftlich völlig gleiche Auswirkung auf alle Unternehmen sei bei keiner Art der Umsatzsteuer möglich. Um die möglichste Steuergerechtigkeit der Umsatzsteuer habe der Gesetzgeber sich seit dem Bestehen dieser Steuer ständig bemüht. Würdige man sein Bemühen in seiner Gesamtheit und geschichtlichen Entwicklung, so habe er sachliche und nicht willkürliche Überlegungen angestellt, wenn er außer der Forderung nach Steuergerechtigkeit auch den Erfordernissen der Einfachheit, Klarheit und Ergiebigkeit Rechnung getragen habe.

Das gegenwärtige System der Umsatzsteuer sei besonders geeignet, durch Vergünstigungen den Mittelstand zu fördern; das habe der Gesetzgeber in weitem Umfange getan. Nach der Statistik für 1962 seien von 3 Millionen Unternehmen rund 1,4 Millionen von der Umsatzsteuer überhaupt befreit. Auch den übrigen mittelständischen Unternehmen seien weitgehend Vergünstigungen eingeräumt worden. Die durchschnittliche Umsatzsteuerbelastung der Gesamtwirtschaft betrage deshalb nur 2,3%, die der Industrieproduktion 2,73%. Die Umsatzsteuer sei als krisenfeste Steuer unentbehrlich. Daß die Ware, die mehrmals umgesetzt werde, höher mit Umsatzsteuer belastet sei als die weniger häufig umgesetzte, sei nur eine Möglichkeit unter anderen; auch das Gegenteil sei wegen der Verschiedenheit der Handels- und Erzeugerspannen, des Einkaufs- und Verkaufswertes eines Produktes möglich.

Die in Aussicht genommene Nettoumsatzsteuer sei zwar wettbewerbsneutraler als die jetzige Umsatzsteuer, aber nicht wettbewerbsneutral schlechthin und habe wieder andere Nachteile. So verdoppele sie die Aufzeichnungspflicht des Unternehmens, zwinge es zur Ausstellung schriftlicher Rechnungen und belaste damit gerade die kleinen und mittleren Betriebe durch Buchhaltungsarbeiten außerordentlich, nicht dagegen die großen Unternehmen mit einer bereits voll ausgebauten Buchführung.

Maßnahmen des Phasenausgleichs über die bereits geltenden hinaus seien dort möglich, wo die Kumulationswirkung der Umsatzsteuer konkret zu erkennbaren schwerwiegenden Benachteiligungen einstufiger Unternehmen führe.

Die Organschaft folge aus dem System der Allphasenumsatzsteuer und sei daher gleichfalls verfassungsmäßig.

2. Eine Anzahl von Unternehmen, die nicht als Einheitsunternehmen aufgebaut,

sondern in einzelne juristische Personen (Organgesellschaften) gegliedert sind, haben die Organschaft als verfassungsgemäß verteidigt. Ihre Beseitigung bei gleichzeitiger Aufrechterhaltung des gegenwärtigen Umsatzsteuersystems würde die Einheitsunternehmen begünstigen und dazu führen, daß die durch die Beseitigung benachteiligten Konzerne zur Struktur des Einheitsunternehmens übergingen und dadurch der umsatzsteuerlichen Mehrbelastung wieder entrinnen würden; damit würde den Beschwerdeführerinnen nicht geholfen. Eine solche Entwicklung würde sich auch von der den Grundsätzen der freiheitlichen wirtschaftlichen Ordnung entsprechenden Dezentralisation entfernen, da die „Diskussionsebene" zwischen Mutter- und Tochtergesellschaften liberaler sei als die innerhalb eines Einheitsunternehmens. Die wirtschaftliche Transparenz sei nach den neuen aktienrechtlichen Vorschriften auch bei in selbständige Gesellschaften aufgegliederten Unternehmen gewährleistet.

Die Gründe für die Organschaft seien nicht weniger sachlich als die für das ganze System. Der innerhalb eines Organkreises gezahlte Preis sei nicht marktgerecht, sondern manipuliert und daher kein praktikabler Besteuerungsmaßstab. Der wirtschaftliche Unterschied zwischen dem Leistungsaustausch innerhalb eines Organkreises und dem unter selbständigen einstufigen Unternehmen rechtfertige nicht nur, sondern fordere sogar eine verschiedene umsatzsteuerliche Behandlung. Andererseits sei der Leistungsaustausch innerhalb eines Organkreises dem Leistungsaustausch innerhalb eines mehrstufigen Einheitsunternehmens bei wirtschaftlicher Betrachtung gleich und dürfe daher nicht nur, sondern müsse auch umsatzsteuerlich gleich behandelt werden.

IV

Zu den finanzwissenschaftlichen und den betriebswirtschaftlichen Fragen haben der Professor der Finanzwissenschaft Dr. Schmölders als gerichtlicher Sachverständiger und die Professoren der Betriebswirtschaftslehre Dr. Pohmer und Dr. Hax als Beistände der Beschwerdeführerinnen und der Bundesregierung Stellung genommen.

Die Zulässigkeit der Verfassungsbeschwerden ist in dem Urteil vom 6. Mai 1964 (BVerfGE 18, 1) ausgesprochen.

B.

Die Verfassungsbeschwerden können im Ergebnis keinen Erfolg haben.

I

1. Das Grundgesetz hat die gegenwärtige Ausgestaltung der Umsatzsteuer nicht schon als materiell verfassungsmäßig anerkannt. Die Art. 106 Abs. 1 und 108 Abs. 1, in denen die Umsatzsteuer namentlich aufgeführt ist, enthalten außer der ausdrücklichen Regelung der Verwaltung und der Verteilung des Steueraufkommens allenfalls eine Billigung ihrer Struktur im großen; sie stellen klar, daß die Erhebung einer Steuer, die ihrem Wesen nach Umsatzsteuer ist, also hauptsächlich die von Unternehmen getätigten Umsätze trifft, nicht verfassungswidrig ist. Die Ausprägung dieser Steuer im einzelnen, insbesondere die hier von den Beschwerdeführerinnen beanstandete Ungleichheit, ist damit noch nicht der verfassungsrechtlichen Nachprüfung entzogen.

2. Auch die bisherige Rechtsprechung des Bundesverfassungsgerichts steht der

von den Beschwerdeführerinnen erbetenen verfassungsrechtlichen Nachprüfung nicht entgegen. Allerdings hat das Bundesverfassungsgericht seinen Entscheidungen auf dem Gebiete des Umsatzsteuerrechts, insbesondere zur Gültigkeit der Ermächtigung in §§ 8 und 18 Abs. 1 Nr. 1 UStG (BVerfGE 7, 282), zur Weitergeltung der Zusatzsteuer in der Textilwirtschaft (BVerfGE 12, 341) sowie zum Ausschluß eines besonderen Fabrikationsunternehmens von der Großhandelsvergünstigung (BVerfGE 19, 64) das geltende Umsatzsteuersystem zugrunde gelegt. Indessen handelte es sich damals nicht um denselben Gegenstand wie jetzt; es ging um klar begrenzte Einzelfragen aus dem Umsatzsteuerrecht, die für sich entschieden werden konnten. Aus diesem Anlaß das Gesamtproblem der Verfassungsmäßigkeit des geltenden Umsatzsteuersystems unter dem Gesichtspunkt der Gleichheit aufzurollen, hätte eine Ausweitung des Prozeßstoffes bedeutet, die weder dem Willen der damaligen Prozeßbeteiligten entsprochen hätte noch — angesichts der Bedeutung und Schwierigkeit der hierbei auftretenden Probleme — sachdienlich gewesen wäre (vgl. BVerfGE 6, 273 [282]).

II.

1 Der an den Gleichheitssatz gebundene Gesetzgeber kann grundsätzlich selbst diejenigen Sachverhalte auswählen, an die er dieselbe Rechtsfolge knüpfen, die er also im Rechtssinne als „gleich" ansehen will. Da die Sachverhalte in der Lebenswirklichkeit sich nie völlig gleichen, müssen gewisse Verschiedenheiten stets vernachlässigt werden. Der Gesetzgeber muß aber seine Auswahl sachgerecht treffen; es kommt darauf an, ob die Unterschiede in den zu regelnden Sachverhalten „für eine am Gerechtigkeitsgedanken orientierte Betrachtungsweise" so erheblich sind, daß ihre Außerachtlassung als willkürlich bezeichnet werden müßte (BVerfGE 1, 14 [52]; seitdem ständige Rechtsprechung). Diese Grundsätze gelten in besonderem Maße für Steuergesetze; da sie einen besonders empfindlichen Eingriff in die Vermögens- und Rechtssphäre der Steuerpflichtigen enthalten, müssen sie dem Gedanken einer möglichst gleichmäßigen Belastung aller Steuerpflichtigen besonders sorgfältig Rechnung tragen.

Andererseits umfassen sie in der Regel Massenvorgänge des Wirtschaftslebens; daher müssen sie, um praktikabel zu sein, die Sachverhalte, an die sie dieselben steuerrechtlichen Folgen knüpfen, typisieren und damit in weitem Umfange die Besonderheiten nicht nur des einzelnen Falles, sondern auch ganzer Gruppen vernachlässigen (BVerfGE 13, 331 [341]). Eine gewisse ungleiche wirtschaftliche Auswirkung auf die einzelnen Steuerschuldner und ihre Wettbewerbslage ist daher bei Steuergesetzen unvermeidbar und hinzunehmen. Jede Steuer greift irgendwie in das freie Spiel der wirtschaftlichen Kräfte ein; eine Steuer, die in jeder Hinsicht völlig wettbewerbsneutral wäre, gibt es nicht und ist kaum denkbar.

Die Gestaltungsfreiheit des Steuergesetzgebers ist aber nicht unbeschränkt; gewisse äußerste Grenzen sind auch ihm gesetzt. Die wirtschaftlich ungleiche Wirkung einer Regelung auf die Steuerzahler darf ein gewisses Maß nicht übersteigen. Die steuerlichen Vorteile der Typisierung müssen im rechten Verhältnis zu der mit der Typisierung notwendig verbundenen Ungleichheit der steuerlichen Belastung stehen. Nur dann ist diese Ungleichheit

von den Betroffenen hinzunehmen. Nur geringfügige oder nur in besonderen Fällen auftretende Ungleichheiten sind freilich unbeachtlich (BVerfGE 13, 331 [341]). Wirkt sich jedoch ein Steuergesetz, das durch eine besonders weite Fassung des typisierten Sachverhalts äußerlich eine ungleiche Behandlung vermeidet, praktisch dahin aus, daß ganze Gruppen von Steuerpflichtigen wesentlich stärker belastet sind als andere und dadurch in eine empfindlich ungünstigere Wettbewerbslage geraten, so können diese ungleichen Folgen in einem Mißverhältnis zu den mit der Typisierung verbundenen Vorteilen stehen. Ein solches Steuergesetz kann dem Art. 3 Abs. 1 GG widersprechen (vgl. BVerfGE 8, 51 ([64]).

2. Aus dieser Sicht genügt die geltende Ausprägung der Umsatzsteuer in ihrer Grundanlage dem Gleichheitssatz. Der Gesetzgeber durfte als einzigen Steuergegenstand den Außenumsatz auswählen und damit den sog. Innenumsatz von der Steuerpflicht ausnehmen, obwohl beide Umsatzformen gewisse Eigenschaften gemeinsam haben. Es ist auch nicht richtig, daß dieser Steuergegenstand für sich allein schon zu der von den Beschwerdeführerinnen beanstandeten Wettbewerbsverzerrung führt; trotz des gleichen Steuergegenstandes vermeidet auch nach der Ansicht der Beschwerdeführerinnen der Entwurf eines Nettoumsatzsteuergesetzes die von ihnen geltend gemachte Wettbewerbsbenachteiligung.

Ebensowenig ist zu beanstanden, daß der Gesetzgeber das von dem Unternehmen für den Außenumsatz vereinnahmte Entgelt zum Besteuerungsmaßstab genommen und einen festen Steuersatz von regelmäßig 4% festgesetzt hat. Dieses Prinzip verbürgt zunächst ein hohes Maß von Gleichheit: für einen gleich hohen Außenumsatz hat jedes Unternehmen einen gleich hohen Umsatzsteuerbetrag zu entrichten.

3. Dabei bleibt der Grad der im einzelnen Unternehmen jeweils erzielten Wertsteigerung des umgesetzten Gegenstandes außer Betracht. Diese Regelung begünstigt grundsätzlich und tendenziell die mehrstufigen gegenüber den einstufigen Unternehmen im wirtschaftlichen Wettbewerb. Darüber besteht Einverständnis.

a) Die Kette von Fertigungs- und Handelsstufen (Gliedern), die ein Produkt auf dem Wege zum Endabnehmer regelmäßig durchläuft, beginnt mit der Urproduktion, umfaßt die vielfachen Stufen der Weiterverarbeitung sowie den Handel. Je mehr Glieder dieser Kette durch — umsatzsteuerpflichtige — Außenlieferungen verbunden sind, desto höher wird es in der Regel mit Umsatzsteuer belastet sein; anders ausgedrückt: ein desto höherer Betrag an Umsatzsteuer muß weitergewälzt werden. Je mehr Glieder dagegen in ein und demselben — „produktionstieferen“ — Unternehmen zusammengefaßt sind, so daß der Übergang von einem Glied der Kette zum anderen nur eine — umsatzsteuerfreie — Innenlieferung darstellt, desto geringer wird gewöhnlich die Belastung mit Umsatzsteuer (der weiterzuwälzende Betrag an Umsatzsteuer) sein.

Die Vielgestaltigkeit der wirtschaftlichen Wirklichkeit läßt es freilich nicht immer zu, die einzelnen Glieder (Fertigungsstufen) klar voneinander abzugrenzen und damit die einstufigen von den mehrstufigen Unternehmen deutlich zu scheiden. Doch gibt es sicher Unterneh-

mensgebilde, die aus mehreren — unter Umständen zahlreichen — einzelnen Betrieben oder Betriebsabteilungen bestehen, in denen auf Grund von technisch aufeinanderfolgenden oder sich ergänzenden Fertigungsvorgängen (d. h. einer „vertikalen Konzentraktion") zahlreiche Glieder einer zusammenhängenden Produktionskette vereint sind; diese Unternehmen besitzen eine große „Produktionstiefe". Es gibt aber auch — möglicherweise weniger kapitalkräftige — Unternehmen von geringerer Produktionstiefe, die sich auf eine Fertigungsstufe (unter Umständen auf wenige Fertigungsstufen) beschränken und den Anschluß an die nächste Fertigungsstufe nur durch eine Außenlieferung bewirken können.

b) Die mehrstufigen — produktionstiefen — Unternehmen vermeiden für die Weitergabe einer Ware von einem Glied der Herstellungskette zu den nächsten Außenlieferungen und beschränken sich insoweit auf Innenlieferungen. Damit ersparen sie eine Belastung der Erzeugerkette mit Umsatzsteuer, die im Preise weitergewälzt werden müßte, und damit Selbstkosten. Dagegen müssen einstufige Unternehmen, wenn sie ihre Ware innerhalb einer sonst gleichen Produktionskette an ein anderes — meist einstufiges — Unternehmen weitergeben, eine — umsatzsteuerpflichtige — Außenlieferung vollziehen. Ein Enderzeugnis, an dessen Herstellungskette mehrere einander beliefernde einstufige Unternehmen beteiligt sind, ist deshalb mit höherer Umsatzsteuer belastet und betriebswirtschaftlich nur mit höheren umsatzsteuerlich bedingten Selbstkosten herzustellen als ein gleichartiges Gut, welches — bei sonst gleicher Art der Herstellung — lediglich durch ein oder wenige mehrstufige Unternehmen hergestellt ist. Die mehrstufigen Unternehmen sind also, von der umsatzsteuerlichen Belastung aus gesehen, im Vorteil vor den einstufigen Unternehmen; ihre geringeren umsatzsteuerlich bedingten Selbstkosten ermöglichen eine Preisunterbietung oder — bei gleichen Entgelten — die Erzielung eines höheren Gewinns.

Dieser mögliche Vorteil der mehrstufigen Unternehmen wächst naturgemäß mit der Höhe des Umsatzsteuersatzes. Die ungleiche Belastung einer Ware mit der Umsatzsteuer fiel bei dem ursprünglichen niedrigen Satz von 0,1% nicht ins Gewicht; mit der fortschreitenden Erhöhung des Steuersatzes auf schließlich 4% ist sie immer fühlbarer geworden.

c) Das Ergebnis, daß das geltende Umsatzsteuersystem die mehrstufigen (produktionstiefen) Unternehmen gegenüber den einstufigen (weniger produktionstiefen) bevorzugt, gilt freilich nicht uneingeschränkt. Die Mehrstufigkeit (größere Produktionstiefe) ist einwandfrei nur für den Fall von Vorteil, daß einer Kette einstufiger Unternehmen ein einzelnes mehrstufiges Unternehmen gegenübersteht. Steht dagegen einer Kette mehrerer einstufiger Unternehmen eine Kette einiger mehrstufiger Unternehmen gegenüber, so ist nicht von vornherein eine Bevorzugung der letzteren Unternehmensart gegeben. Vielmehr hängt es von der Verteilung der jeweiligen Wertschöpfung auf die hintereinandergeschalteten Unternehmen ab, ob die eine oder die andere Unternehmensart stärker belastet ist. Je stärker in einer Kette von mehrstufigen Unternehmen die Wertschöpfung auf die Anfangsglieder der Kette verlagert und je geringer sie damit in den Endgliedern ist, desto eher wird der Vorzug der Mehr-

stufigkeit gemindert oder aufgehoben; es ist sogar möglich, daß die Herstellung und der Vertrieb eines Produktes durch mehrstufige Unternehmen eine größere umsatzsteuerliche Belastung herbeiführt, als wenn sie durch einstufige Unternehmen erfolgt.

Eine Gesamtbetrachtung, wie sie insbesondere in den fachwissenschaftlichen und steuerpolitischen Erörterungen ihren Ausdruck findet, zeigt jedoch, daß jedenfalls ganz überwiegend die einstufigen Unternehmen benachteiligt sind und ihre größere Belastung durch zweifellos auch vorhandene gegenteilige Möglichkeiten nicht aufgewogen wird.

4. Gegenüber diesem Mangel an Wettbewerbsneutralität hat die geltende Ausprägung der Umsatzsteuer unleugbar auch große Vorteile. Sie ist an Klarheit der Regelung und Einfachheit der Handhabung sowohl für die Finanzverwaltung als für die steuerpflichtigen Unternehmen jeder anderen möglichen Art einer Umsatzsteuer überlegen. Auch die zahlreichen Befreiungen und Vergünstigungen sind nicht geeignet, dieses Ergebnis in Frage zu stellen; denn sie gelten nur innerhalb eines umgrenzten Bereichs und lassen die Steuerpflicht der außerhalb ihres Geltungsbereichs liegenden Umsätze unberührt. Diese besonderen Vorzüge haben auch eine besonders hohe Nettoergiebigkeit zur Folge.

Eine relativ hohe Krisenfestigkeit eignet allerdings jeder Art von Umsatzsteuer und kommt daher als besonderer Vorteil ihrer jetzt geltenden Ausprägung nicht in Betracht.

5. Gegenüber diesem Vorteil fällt aber ins Gewicht, daß die Benachteiligung der einstufigen Unternehmen gegenüber den mehrstufigen sich nicht auf Sonderfälle beschränkt, sondern eine erhebliche Gruppe von Unternehmen umfaßt.

Die Benachteiligung ist auch nicht nur geringfügig, sondern hat ein für die Wettbewerbslage der betroffenen Unternehmen nicht zu übersehendes Gewicht. Die umsatzsteuerliche Belastung kann für die Wettbewerbslage von Unternehmen von Bedeutung sein; dies ergibt sich mittelbar schon daraus, daß der Gesetzgeber und die in Frage kommenden Steuerpflichtigen die vielfachen Umsatzsteuervergünstigungen und -befreiungen als ein geeignetes Mittel ansehen, um wirtschafts- oder sozialpolitische Ziele zu erreichen.

a) Es mag sein, daß die industriellen Unternehmen wegen gewisser Steuerbefreiungen, insbesondere für die Ausfuhrlieferungen (§ 4 Nr. 3 UStG), im Durchschnitt für den einzelnen Umsatz tatsächlich nicht 4%, sondern nur 2,7% Umsatzsteuer aufzubringen haben; dieser durchschnittlich geringere Steuersatz ist aber für die Wettbewerbslage gerade der einstufigen Unternehmen gegenüber den mehrstufigen nicht von ausschlaggebender Bedeutung. Auf der anderen Seite nimmt der Konkurrenzdruck der durch die geltende Umsatzsteuer bevorzugten mehrstufigen Unternehmensgebilde im Laufe der Zeit immer weiter zu; ihr Umsatz und ihr Marktanteil wachsen in der Regel stärker als die der anderen Unternehmen. Ein Schutz des einstufigen Unternehmens durch Kartellpreise ist durch das Gesetz gegen Wettbewerbsbeschränkungen weitgehend untersagt.

b) Demgegenüber bringen gewisse entgegenwirkende Momente keine wesentliche Milderung. Freilich ist die Umsatz-

steuer auf Abwälzung angelegt; in der Regel wird sie auch abgewälzt werden. Diese Möglichkeit, die sie mit allen sonstigen Selbstkosten teilt, schließt aber die Erfahrungstatsache nicht aus, daß die Konkurrenzfähigkeit des Unternehmens in weitestem Umfange gerade von seinen Selbstkosten abhängt. Der als Umsatzsteuer abzuführende Betrag ist allerdings immer nur ein Kostenfaktor unter zahlreichen anderen und viel wesentlicheren, deren Höhe dazu noch von Betrieb zu Betrieb schwankt; das Besondere der Umsatzsteuer besteht aber gerade darin, daß sie dem Unternehmen vom Staat auferlegt ist, während die anderen Kostenfaktoren, wie etwa die Aufwendungen für das Anlagekapital, die Vorprodukte oder die Arbeitskräfte, im wesentlichen von staatlichen Maßnahmen unabhängig sind und auch in weitem Umfange von den einzelnen Unternehmen beeinflußt werden können, z. B. durch die Auswahl des Standortes oder des Herstellungsverfahrens. Zweifellos gibt es zahlreiche Fabrikate, deren Absatz nicht allein durch den Preis, sondern durch andere Momente, so etwa den Geschmack, die Bequemlichkeit, Brauchbarkeit oder Gewohnheit, bestimmt wird; andererseits gilt dies nicht allgemein. Keinesfalls ist der Preis aber als ein entscheidender Faktor im Wettbewerb auszuschließen. Höhere Gewinne, die die mehrstufigen Unternehmen durch niedrigere, umsatzsteuerlich bedingte Selbstkosten erzielen, werden in gewissem Umfange durch Gewinnsteuern wieder weggesteuert, jedoch nie vollständig und nicht, soweit etwa Steuervergünstigungen Platz greifen; soweit mehrstufige Unternehmen nur geringe oder keine Gewinne erzielen, ist für einen solchen Ausgleich nur ein geringer oder überhaupt kein Raum. Die zahlreichen im Umsatzsteuergesetz enthaltenen Steuerbefreiungen und -ermäßigungen kommen nur bestimmten Wirtschaftszweigen oder -gruppen, nicht aber allgemein gerade den einstufigen Industrieunternehmen im Unterschied zu den mehrstufigen zugute. Daß das Risiko und die Krisenanfälligkeit der mehrstufigen Unternehmen höher seien als die der einstufigen, läßt sich generell nicht feststellen.

c) Auch die Bundesregierung und der Bundesminister der Finanzen haben immer wieder auf die mangelnde Wettbewerbsneutralität der Umsatzsteuer hingewiesen und zu erkennen gegeben, daß die Beseitigung dieses Mangels ein vordringliches wirtschaftliches und steuerpolitisches Ziel sei.

In der „Denkschrift über eine Änderung des Umsatzsteuergesetzes“ vom 6. Dezember 1955 (BTDrucks. II/1924, S. 7) erklärt der Bundesminister der Finanzen:

„. . . Unternehmen, die mehrere Wirtschaftsstufen in sich vereinigen, haben weniger Umsatzsteuer zu zahlen als die entsprechenden einstufigen Unternehmen zusammen. Den ersteren erwächst daraus ein wettbewerbsmäßiger Vorteil, weil die von ihnen abgesetzten Waren geringer mit Umsatzsteuer belastet sind als die der letzteren.“

In der vom Bundesminister der Finanzen herausgegebenen „Denkschrift über die Möglichkeiten einer Verbesserung der Umsatzbesteuerung“ vom 20. Dezember 1958 (BTDrucks. III/730, S. 8) heißt es:

„Die Kumulation kann bei konkurrierenden Waren zu einer Verletzung der Wettbewerbsneutralität führen . . .“
„Die Einsparung einer Umsatzphase

bringt — im Vergleich zum Konkurrenzunternehmen, das auf die entsprechende Umsatzphase nicht verzichten kann — einen Steuervorteil von normalerweise 4 v. H. des Umsatzwertes der Phase. Der Vorteil spielt mithin in der Kostenkalkulation durchaus eine Rolle."

Weiter hat der Bundesminister der Finanzen im Deutschen Bundestag am 15. Februar 1963 (BT IV 1961 Sten.Ber. S. 2793 [B]) erklärt:

„. . . Wem es also gelingt, Wirtschaftsstufen auszuschalten oder mehrere Stufen in seinem Unternehmen zusammenzufassen, der kann dadurch Umsatzsteuer sparen. Unsere derzeitige Umsatzsteuer begünstigt daher die vertikale Konzentration . . ."

Die Begründung des Entwurfs eines Umsatzsteuergesetzes vom 30. Oktober 1963 (BTDrucks. IV/1590, S. 20) sagt:

„. . . Wer mithin im Rahmen des Produktions- und Verteilungsprozesses eine Umsatzstufe oder sogar mehrere Umsatzstufen einsparen kann, erhält im Vergleich zu seinem Konkurrenten, der auf die entsprechende Umsatzstufe angewiesen ist, einen umsatzsteuerlich bedingten Kostenvorteil . . ."

Auch der „Bericht über das Ergebnis einer Untersuchung der Konzentration in der Wirtschaft" vom 29. Februar 1964 (BT-Drucks. IV/2320, S. 53 und 54) bemängelt das geltende Umsatzsteuersystem:

„. . . Damit hat sich die im System der kumulativen Allphasenumsatzsteuer begründete Wettbewerbsverzerrung zugunsten der mehrstufigen Großunternehmen besonders verstärkt . . ."

„. . . Die konzentrationsfördernde Wirkung des geltenden Umsatzsteuersystems ergibt sich daraus, daß bei Verbindung mehreren Produktions- und Handelsstufen in einem Unternehmen oder in einem umsatzsteuerlichen Organkreis die Umsatzsteuer nur einmal — beim Übergang der Erzeugnisse an Dritte — anfällt . . ."

d) Nach alledem führt das geltende System grundsätzlich und tendenziell dazu, daß die mehrstufigen Unternehmen mit geringeren umsatzsteuerlich bedingten Selbstkosten belastet sind als die einstufigen und daher diesen gegenüber im Wettbewerb bevorzugt werden. Die höhere Belastung mit umsatzsteuerlich bedingten Selbstkosten schmälert die Gewinne der einstufigen und erhöht im Vergleich dazu die der mehrstufigen. In einem solchen Falle stehen dann den einstufigen weniger Mittel als ihren mehrstufigen Konkurrenten für eine insbesondere durch technische Neuerungen etwa gebotene Selbstfinanzierung zur Verfügung; dadurch wird aber grundsätzlich ihre Wettbewerbsfähigkeit auf lange Sicht entscheidend beeinträchtigt werden.

6. Die substantiierten Darlegungen der Beschwerdeführerinnen haben dem Bundesverfassungsgericht die Überzeugung vermittelt, daß auch sie durch die höhere Umsatzsteuerbelastung gegenüber ihren mehrstufigen Konkurrenten erheblich benachteiligt sind.

7. Daß die geltende Ausprägung der Umsatzsteuer, nach der jeder Unternehmer ohne Rücksicht auf den ein- oder mehrstufigen Aufbau (die Produktions-

tiefe) seines Unternehmens für einen gleich hohen Außenumsatz ausnahmslos einen gleich hohen Steuerbetrag zu entrichten hat, die Wettbewerbslage der einstufigen Unternehmen gegenüber den mehrstufigen grundsätzlich schmälert, hat der Gesetzgeber erkannt, aber nicht gebilligt oder auch nur als unabänderlich in Kauf genommen. Vielmehr war er bestrebt, die ungleiche Belastung durch geeignete Maßnahmen zu beheben.

a) Schon das Umsatzsteuergesetz von 1918 gab die Möglichkeit, auch Innenlieferungen zu besteuern. Das Umsatzsteuergesetz von 1932 ermächtigte den Reichsminister der Finanzen, zur Korrektur der Allphasenbesteuerung zu bestimmen,

> „daß nicht jeder steuerpflichtige Umsatz, sondern nur einzelne Umsätze ... besteuert werden mit der Wirkung, daß die vorangegangenen oder folgenden Umsätze ganz oder zum Teil von der Steuer ausgenommen sind (Phasenpauschalierung)".

Beide Möglichkeiten blieben ungenutzt.

Wie bereits erwähnt, hatte das Umsatzsteuergesetz 1934 — bei dem damals geltenden Steuersatz von nur 2% — den Reichsfinanzminister ermächtigt, Maßnahmen zum Ausgleich der verschiedenen Umsatzsteuerbelastung der einstufigen und der mehrstufigen Unternehmen zu treffen. Dieses Verfahren entsprach der mit dem damaligen Staatsrecht vereinbarten Übung im Gesetz selbst nur gewisse Grundsätze festzulegen und die für ihre praktische Durchführung erforderliche Ausgestaltung im einzelnen, dabei aber auch die Anordnung der für besondere Sachverhalte gebotenen Ausnahmen der Exekutive aufzugeben. Der Reichsgesetzgeber hat also nicht für jeden Fall und ausnahmslos die Regelung gewählt, daß jeder Unternehmer ohne Rücksicht auf den besonderen Aufbau seines Unternehmens für den gleich hohen Außenumsatz einen gleich hohen Steuerbetrag zu entrichten habe. Vielmehr hat er die verschiedene umsatzsteuerliche Belastung der einstufigen und der mehrstufigen Unternehmen gerade nicht in jedem Falle gebilligt und durch eine Ermächtigung dem Reichsminister der Finanzen einen Ausgleich aufgetragen.

Von dieser Ermächtigung machte der Reichsfinanzminister für die Textilwirtschaft durch eine Zusatzsteuer für Spinnwebereien Gebrauch; diese Zusatzsteuer besteht noch heute (BVerfGE 12, 341). Bei den anderen Wirtschaftszweigen, z. B. auf dem Gebiet der eisenverarbeitenden Industrie, waren vor 1945 Ausgleichsmaßnahmen nicht erforderlich, weil diese Wirtschaftszweige bereits durch verbandsmäßige Preisregelungen einen Ausgleich der Umsatzsteuerbelastung zwischen ein- und mehrstufigen Unternehmen herbeigeführt hatten.

b) Der Bundesgesetzgeber hat — bei gleichzeitiger Erhöhung des Steuersatzes auf 4% — diese Ermächtigung erneuert, indem er in § 1 Nr. 10 des Gesetzes zur Änderung des Umsatzsteuergesetzes und des Beförderungssteuergesetzes vom 28. Juni 1951 (BGBl. I S. 402) den § 18 UStG neu gefaßt und für den hier in Frage kommenden Ausgleich — auszugsweise — bestimmt hat:

„Durchführung

§ 18

(1) Die Bundesregierung wird ermächtigt, durch Rechtsverordnungen

1. zur Durchführung dieses Gesetzes die in . . . § 8 . . . vorgesehenen Bestimmungen zu erlassen . . .
. . ."

Damit hat auch der Bundesgesetzgeber genügend deutlich zum Ausdruck gebracht, daß er die Außenumsätze von einstufigen und von mehrstufigen Unternehmen umsatzsteuerlich nicht ausnahmslos gleich, sondern gegebenenfalls verschieden behandelt wissen will.

8. Diese Konzeption des Gesetzgebers hatte also ein Umsatzsteuergesetz geschaffen, das ein relativ ausgewogenes System des ganzen Umsatzsteuerrechts erstrebte. Die Verwirklichung der Konzeption auf dem eingeschlagenen Wege ist jedoch gescheitert: Die erteilte Ermächtigung genügte den Erfordernissen des Art. 80 Abs. 1 Satz 2 GG nicht und wurde vom Bundesverfassungsgericht in seiner Entscheidung vom 5. März 1958 (BVerfGE 7, 282) für nichtig erklärt. Der danach als gültig bestehengebliebene Wortlaut des Gesetzes enthält nicht mehr die rechtliche Möglichkeit, die verschiedene Belastung der einstufigen und der mehrstufigen Unternehmen im Verordnungswege auszugleichen, und stellt ausnahmslos die Außenumsätze der einstufigen denen der mehrstufigen Unternehmen gleich. Eine solche Regelung widerspricht aber den eigenen Vorstellungen des Gesetzgebers, der gerade eine solche unabänderliche Gleichstellung vermeiden, die ungleiche Behandlung der Außenumsätze der beiden Unternehmensgruppen ermöglichen und damit eine gerechtere umsatzsteuerliche Belastung herbeiführen wollte. Der jetzige Wortlaut des Gesetzes wird also den Vorstellungen, die der Gesetzgeber selbst von einer dem Gleichheitssatz genügenden Belastung der ein- und mehrstufigen Unternehmen hatte, nicht mehr gerecht.

9. Durch die bezeichnete Entscheidung des Bundesverfassungsgerichts ist aber die ursprüngliche Konzeption des Gesetzgebers nicht etwa hinfällig geworden. Sie betraf nicht den materiellen Gehalt seiner Konzeption, sondern hat nur den Weg, auf dem der Gesetzgeber seine Absicht verwirklichen wollte, als verfassungsrechtlich ungangbar bezeichnet.

Der Gesetzgeber selbst hat auch daraufhin seine ursprüngliche Absicht, ein ausgewogenes System der umsatzsteuerlichen Belastung zu schaffen, nicht aufgegeben und nicht endgültig die Außenumsätze der einstufigen und der mehrstufigen Unternehmen umsatzsteuerlich gleich behandeln wollen. Im Gegenteil hat er in seinen Bestrebungen, einen Ausgleich zu schaffen, nie nachgelassen.

Eine vom Bundesminister der Finanzen beauftragte, aus Steuersachverständigen zusammengesetzte Kommission erstattete im Oktober 1959 den „Bericht der Kommission zur technischen Prüfung der Umsatzsteuer-Reformvorschläge", der im Ergebnis von einer Reform abriet. Im August 1960 legte der Bundesminister der Finanzen eine „Studie zu einer Mehrwertsteuer mit Vorsteuerabzug in der Form eines Gesetzentwurfes mit Erläuterungen" der Öffentlichkeit vor. Die Auswirkungen dieser Besteuerungsform sind darin erörtert. Im Jahre 1962 betrafen zwei große Anfragen im Bundestag die Umsatzsteuerreform (BTDrucks. IV/548 und 648). Aus der Mitte des Bundestages wurde ein Gesetzentwurf über ein neues Umsatzsteuergesetz, das auf dem Prinzip der Mehrwertsteuer mit Vorsteuerabzug beruhte, eingebracht (BTDrucks. IV/660). Im Herbst 1962 schlug die EWG-Kom-

mission auf Grund mehrjähriger Untersuchungen dem Rat den Erlaß einer von ihr entworfenen „Richtlinie zur Harmonisierung der Rechtsvorschriften der einzelnen Mitgliedstaaten betreffend die Umsatzsteuer" vor, nach der die Mitgliedstaaten stufenweise ein gemeinsames Mehrwertsteuersystem einführen sollen. Bundestag und Bundesrat haben diesem ihnen von der Bundesregierung zugeleiteten Vorschlag zugestimmt.

Schließlich suchte die Bundesregierung mit dem Entwurf eines Umsatzsteuergesetzes vom 30. Oktober 1963 (BTDrucks. IV/1590) eine Abhilfe zu schaffen durch die Einführung einer „Mehrwertsteuer mit Vorsteuerabzug": Wie bisher sollte Steuerschuldner der die Leistung erbringende Unternehmer und alleiniger Steuergegenstand sein Außenumsatz sein; Besteuerungsmaßstab sollte das für den Außenumsatz gezahlte Entgelt und der Steuersatz ein fester Hundertsatz dieses Entgeltes bleiben. Das entscheidend Neue lag darin, daß unter Erhöhung des Steuersatzes auf 10% der Steuerschuldner von der danach sich ergebenden Steuerschuld — vereinfacht ausgedrückt — die Umsatzsteuerbeträge, die ihm von anderen Unternehmern im gleichen Zeitraum in Rechnung gestellt worden waren, sollte abziehen dürfen. Dieser Entwurf wurde vom Bundestag seinerzeit nicht mehr verabschiedet. In der laufenden Legislaturperiode ist aus der Mitte des Bundestags ein Entwurf vom 24. November 1965 (BT-Drucks. V/48) mit demselben Inhalt unter der Bezeichnung „Nettoumsatzsteuer" — ohne gesonderte Begründung — eingebracht worden. Über ihn beraten zur Zeit die zuständigen Ausschüsse.

10. Genügt demnach das Umsatzsteuergesetz in seiner geltenden Fassung der vom Gesetzgeber selbst gewünschten Steuergerechtigkeit insoweit nicht, als es die Außenumsätze der einstufigen den Außenumsätzen der mehrstufigen Unternehmen ausnahmslos gleichstellt, so kann doch jedenfalls zur Zeit weder das Gesetz für nichtig erklärt noch eine Grundrechtsverletzung festgestellt werden. Dies gilt auch für die sonstigen von den Beschwerdeführerinnen gerügten Verfassungsverstöße, da sie im wesentlichen mit denselben Erwägungen begründet werden.

Die besonders große Bedeutung, die das Umsatzsteuergesetz für die Einnahmen des Bundes, aber auch für die Selbstkosten der Unternehmen und die allgemeine Preisgestaltung hat, läßt es jedenfalls zur Zeit nicht zu, das ganze Gesetz nur deshalb für nichtig zu erklären, weil besondere, wenn auch nicht unbedeutende Gruppen gegenüber anderen viel zahlreicheren Gruppen ungleich behandelt sind; dies wäre vielleicht in einfach liegenden Fällen möglich, würde hier aber zu dem unerträglichen Ergebnis führen, daß dem Gesetz in dem unverhältnismäßig viel größeren Bereich die Geltung versagt werden würde, der von der hier zu entscheidenden Frage überhaupt nicht berührt ist. Eine Nichtigerklärung des ganzen Gesetzes haben die Beschwerdeführerinnen auch nicht begehrt.

Ebensowenig geht es aber an, das Gesetz nur in dem beschränkten Umfange, in dem die hier erörterte ungleiche Belastung Bedeutung hat, für nichtig zu erklären. Eine solche Begrenzung der Nichtigkeit wäre nur theoretisch möglich. Praktisch läßt sich bei dem umfassenden Steuergegenstand eine Formulierung, die den nichtigen Teil von dem gültigen justiziabel abgrenzen würde, nicht finden.

Der Gesetzgeber selbst konnte bei der Unübersichtlichkeit und Vielschichtigkeit

der tatsächlichen wirtschaftlichen Zusammenhänge und der Schwierigkeit, eine neue befriedigende Regelung zu finden, nicht wie in anderen, einfach liegenden Fällen durch eine rasche Entscheidung die Gleichheit in der einen oder anderen Richtung herstellen. Es blieb ihm keine andere Wahl, als das Umsatzsteuergesetz in seiner durch den Wegfall der Ausgleichsermächtigung allerdings lückenhaft gewordenen Gestalt zunächst weiterbestehen zu lassen und so Zeit zu gewinnen, eine gesetzliche Regelung zu finden, die das gestörte Gleichgewicht der umsatzsteuerlichen Belastung wiederherzustellen geeignet war.

Schließlich ist für die einstufigen Unternehmen wie die Beschwerdeführerinnen die zeitweise Weitergeltung des Gesetzes bei der gegebenen Situation nicht völlig unerträglich. Daß auch sie wie die Vielzahl der Unternehmen, für die die hier zu entscheidende Frage ohne Bedeutung ist, zunächst weiter wie bisher ihre Umsätze zu versteuern haben, ist eine Selbstverständlichkeit. Nur die Verbesserung ihrer Wettbewerbslage, um die es den Beschwerdeführerinnen eigentlich geht und die innerhalb des geltenden Systems wahrscheinlich nur durch eine irgendwie gestaltete zusätzliche Besteuerung der mehrstufigen Unternehmen ermöglicht werden könnte, tritt nicht alsbald ein. Indes ist sie nur hinausgeschoben; sie wird aber, wie noch zu erörtern ist, in absehbarer Zeit verwirklicht werden. Diese sichere Aussicht allein muß sich schon heute dahin auswirken, daß ihre Wettbewerbslage, auf lange Sicht gesehen, verbessert erscheint.

11. Muß hiernach das Umsatzsteuergesetz in seiner gegenwärtigen unvollkommenen Gestalt zunächst noch Bestand haben, so sind seiner Weitergeltung, soweit es den Außenumsatz der einstufigen dem der mehrstufigen Unternehmen starr gleichsetzt, doch zeitliche Grenzen gesetzt.

Durch die Entscheidung des Bundesverfassungsgerichts vom 5. März 1958, die die zuvor nicht eindeutig erkennbare Unvereinbarkeit der Ausgleichsermächtigung mit Art. 80 Abs. 1 Satz 2 GG ausgesprochen hat, war der Gesetzgeber vor eine neue und unerwartete Situation gestellt worden: Das gewählte Mittel, mit dem er eine nach seinen Vorstellungen gerechte Besteuerung der Außenumsätze der einstufigen und mehrstufigen Unternehmen erreichen wollte, war ihm genommen. Er mußte einen anderen, mit der Verfassung vereinbarten Weg suchen, um sein Ziel zu erreichen, sei es, indem er eine neue den Erfordernissen des Art. 80 Abs. 1 Satz 2 GG genügende Ermächtigung erteilte, sei es, daß er andere gesetzgeberische Maßnahmen ergriff.

In welchem Umfange ein Ausgleich zwischen der verschiedenen umsatzsteuerlichen Belastung überhaupt erforderlich ist, um eine vernünftige Wettbewerbslage zwischen einstufigen und mehrstufigen Unternehmen sicherzustellen, liegt wegen der nicht leicht überschaubaren, vielschichtigen wirtschaftlichen Zusammenhänge innerhalb der einzelnen Wirtschaftszweige keineswegs klar auf der Hand; dies erhellt schon daraus, daß auch von der Ermächtigung der §§ 8 und 18 UStG nur sehr sparsam Gebrauch gemacht worden war. Die nach Klärung dieser Umstände erforderliche rechtliche Regelung begegnet weiteren, schwer überwindbaren Schwierigkeiten; eine Änderung der Grundstruktur des Gesetzes kann sehr weittragende und nicht immer sicher voraussehbare Folgen zeitigen. Wie

groß die tatsächliche und rechtliche Differenziertheit der ganzen Materie ist, tritt erneut in den fachwissenschaftlichen Erörterungen und den gesetzgeberischen Beratungen in Erscheinung, die eine bessere Wettbewerbsneutralität durch die Einführung des Vorsteuerabzugs erstreben.

Die Erörterungen aller dieser Umstände brachten nur auf bestimmten Teilgebieten, wie z. B. dem des Großhandels, einen Ausgleich, führten aber letztlich zu der Überzeugung, daß im Rahmen des geltenden Systems keine Möglichkeiten bestünden, allgemein, etwa durch eine zusätzliche Besteuerung der mehrstufigen Unternehmen, die ungleiche Belastung mit Umsatzsteuer zu beseitigen oder wenigstens auf ein erträgliches Maß herabzusetzen. Daher hat sich der Gesetzgeber dazu entschlossen, das bisherige System der Allphasenbruttoumsatzsteuer überhaupt aufzugeben und eine Nettoumsatzsteuer mit Vorsteuerabzug einzuführen, über die er zur Zeit berät. Dieses neue Umsatzsteuersystem ist nach den übereinstimmenden Angaben der vom Gericht gehörten Sachkundigen geeignet, die Wettbewerbsneutralität der Umsatzsteuer wesentlich zu verbessern.

Naturgemäß bringt eine solche Änderung des ganzen Systems die zeitraubende Aufgabe mit sich, daß die Grundsätze und die zahlreichen Einzelheiten mit Hilfe sachverständiger Stellen in jeder Hinsicht genau durchdacht und ausgearbeitet werden. Eine übereilte Regelung könnte zu nicht abzusehenden Nachteilen, wie etwa Unklarheiten oder neuer Unebenheiten in der Belastung führen, die bei einem Gesetz von der wirtschaftlichen und finanziellen Tragweite des Umsatzsteuergesetzes auch nicht vorübergehend in Kauf genommen werden könnten.

In Anbetracht dieser besonderen und einmaligen Situation muß die dem Gesetzgeber zuzubilligende Frist geräumig bemessen werden. Obgleich seit der Entscheidung des Bundesverfassungsgerichts vom 5. März 1958 mehr als acht Jahre vergangen sind, kann die Frist noch nicht als abgelaufen bezeichnet werden. Dabei geht das Bundesverfassungsgericht davon aus daß der Gesetzgeber die begonnene Reform des Umsatzsteuerrechts ohne andere Verzögerungen als die, die sich aus der Natur der Sache oder aus der gebotenen Rücksicht auf die Steuerharmonisierung im Rahmen der Europäischen Wirtschaftsgemeinschaft ergeben, weiterführt, sie in absehbarer Zeit abschließt und damit die hier erörterte Ungleichheit behebt.

III.

Die vorstehend entwickelten Gründe müssen dazu führen, auch das besondere Institut der Organschaft zeitweise, nämlich bis zum Abschluß der allgemeinen Umsatzsteuerreform, weiterbestehen zu lassen.

1. Die Organschaft ist von der Rechtsprechung der Steuergerichte aus der Systematik des Umsatzsteuerrechts entwickelt worden. Ursprünglich war es selbstverständlich, daß juristische Personen des Privatrechts stets als Unternehmer und damit ihre entgeltlichen Lieferungen an Abnehmer als Außenlieferungen angesehen wurden. Diese Ansicht wurde allmählich aufgelockert und schließlich aufgegeben, weil „die zwingende Logik der wirtschaftlichen Tatsachen dazu nötige“ (Popitz-Kloss-Grabower, Kommentar zum UStG, 3. Aufl. 1928, S. 304). Die Rechtsprechung hat dabei folgende Überlegungen angestellt:

Die umsatzsteuerlichen Begriffe fielen nicht mit Begriffen des bürgerlichen Rechts oder der Gewerbeordnung zusammen, sondern seien besondere „steuerrechtliche Wirtschaftsbegriffe". Das für den Unternehmerbegriff im Sinne des Umsatzsteuergesetzes (§ 2 Abs. 1 Satz 1) erforderliche Begriffsmerkmal der Selbständigkeit bestimme sich daher lediglich nach wirtschaftlichen, nicht nach bürgerlich-rechtlichen Gesichtspunkten. Trotz zivilrechtlicher Selbständigkeit könne danach einer juristischen Person die Unternehmereigenschaft im Sinne des Umsatzsteuergesetzes wegen wirtschaftlicher Unselbständigkeit fehlen. Dies sei der Fall, wenn die Organgesellschaft als Teil eines fremden Gewerbebetriebs einem fremden Willen dergestalt untergeordnet sei, daß sie in ihrer Beteiligung am Wirtschaftsleben nur diesen fremden Willen verwirklichen könne und aufhöre, einen eigenen Willen zu haben. Deshalb sei eine juristische Person dann als unselbständig anzusehen, wenn sie „finanziell, wirtschaftlich und organisatorisch, d. h. völlig" von einem Unternehmer abhängig sei (RFH Slg. Bd. 36, 39 [42 f.]).

Diese zunächst aus den Grundsätzen des Umsatzsteuerrechts von der Rechtsprechung und Rechtslehre entwickelte Rechtsfigur hat das Umsatzsteuergesetz 1934 mit dem bezeichneten Wortlaut als § 2 Abs. 2 Satz 2 ausdrücklich übernommen.

Im Sinne der „Entflechtung" setzte der Kontrollrat für die Zeit vom 1. Januar 1946 ab den § 2 Abs. 2 Nr. 2 UStG „außer Kraft" und erklärte die Lieferungen innerhalb eines Organkreises für umsatzsteuerpflichtig (Art. II des Kontrollratsgesetzes Nr. 15). Da er dabei als beherrschendes Unternehmen ausdrücklich eine „Muttergesellschaft" bezeichnete, ließen die herrschende Lehre und die Rechtsprechung die Organschaft für den Fall bestehen, daß die „Mutter" eine natürliche Person oder eine Körperschaft des öffentlichen Rechts war.

Durch Art. 2 des Neunten Gesetzes zur Änderung des Umsatzsteuergesetzes vom 18. Oktober 1957 (BGBl. I S. 1743) wurde die Organschaft vom 1. April 1958 ab wieder in vollem Umfang eingeführt. Dabei stützte sich der Bundestagsausschuß für Finanz- und Steuerfragen auf den Begriff der Selbständigkeit der gewerblichen oder beruflichen Tätigkeit der Unternehmer, wie er durch die Rechtsprechung des Reichsfinanzhofs entwikkelt war; außerdem wies er auf die „unerfreuliche Lage" hin, die durch die nur teilweise Aufhebung der Organschaft und die mannigfachen Ausnahmen für die entflochtene Industrie (vgl. Verordnungen vom 10. Februar 1953 — BGBl. I S. 17 — und vom 7. Februar 1957 — BGBl. I S. 29 —) entstanden sei. Er hielt „aus systematischen Gründen und wegen der im Umsatzsteuerrecht herrschenden wirtschaftlichen Betrachtungsweise" die Wiedereinführung der Organschaft für notwendig (BTDrucks. II/zu 3511 S. 6). Auf Grund des Ausschußberichts verabschiedete der Bundestag ohne weitere Aussprache das Änderungsgesetz einstimmig (BT II Sten. Ber. S. 12 767 [B]).

Nach dem Gesetz vom 18. Oktober 1957 kam die Organschaft auch den juristischen Personen zugute, an denen das herrschende Unternehmen u. U. nur zu 51% beteiligt war. Das Elfte Gesetz zur Änderung des Umsatzsteuergesetzes vom 16. August 1961 — BGBl. I S. 1330 — engte die Voraussetzungen für das Vorliegen einer Organschaft dahin ein, daß dem herrschenden Unternehmen mehr als 75% der Anteile oder Stimmrechte an der Organgesellschaft gehören müssen.

2. Diese Entwicklung zeigt, daß der Gesetzgeber mit der von den Beschwerdeführerinnen zu I bekämpften Wiederherstellung der Organschaft im Jahre 1957 die Absicht verfolgt hat, die ursprüngliche Systematik des Umsatzsteuergesetzes, die durch die Maßnahmen der Besatzungsmächte gestört war, wiederherzustellen. Nach dieser Systematik liegt ein steuerpflichtiger Umsatz nur dann vor, wenn ein Unternehmer die Lieferung oder Leistung vollbringt; nur ein Unternehmer kann Steuerschuldner sein. Zum Begriff des Unternehmers gehört aber dessen Selbständigkeit; sie fehlt einer juristischen Person, die dem Willen eines — selbständigen — Unternehmers derart untergeordnet ist, daß sie keinen eigenen Willen hat. Dieser Systematik entspricht es, daß der Entwurf eines Nettoumsatzsteuergesetzes die Rechtsfigur der Organschaft beibehält — § 2 Abs. 2 Nr. 2 des Entwurfs eines Umsatzsteuergesetzes (Nettoumsatzsteuer) vom 24. November 1965 (BTDrucks. V/48) in Verbindung mit Entwurf eines Umsatzsteuergesetzes vom 30. Oktober 1963 (BTDrucks. IV/1590 S. 36) —, wobei allerdings ihre den freien Wettbewerb bisher beeinträchtigende Wirkung durch die Einführung des Vorsteuerabzugs entschärft wird.

Mag die Lieferung einer Organgesellschaft innerhalb ihres Organkreises zivilrechtlich auch als Außenlieferung erscheinen, umsatzsteuerrechtlich handelt es sich dabei nach dem Ausgeführten um eine Innenlieferung.

3. Bei seiner Zielsetzung, die Systematik des Umsatzsteuergesetzes wiederherzustellen, durfte der Gesetzgeber die Folge in Kauf nehmen, daß er den Kreis der durch die geltende Gestalt des Umsatzsteuergesetzes Begünstigten erweitert und damit die Wettbewerbslage der einstufigen Unternehmen noch weiter beeinträchtigt hat. Demgegenüber würde die Nichtigerklärung der Organschaft allein unter gleichzeitiger Aufrechterhaltung des Systems im ganzen zu dem unerwünschten Ergebnis führen, daß innerhalb des Bereichs der großen mehrstufigen Unternehmensgebilde die Einheitsgesellschaften vor den Konzernen ohne zureichenden Grund begünstigt und damit wirtschaftlich gleiche Vorgänge nur wegen ihrer formalrechtlich verschiedenen Ausgestaltung verschieden behandelt würden. Daher erscheint es sachgerecht, in die Aufrechterhaltung des Umsatzsteuergesetzes auch die Organschaft einzubeziehen; dies um so mehr, als der Gesetzgeber, wie erwähnt, beabsichtigt, die Rechtsfigur der Organschaft bei der Reform des Umsatzsteuerrechts zu übernehmen.

DEVELOPMENTS IN INTERNATIONAL TAX LAW

UNTERRICHTUNG ÜBER DEN STAND VON DEUTSCHEN DOPPELBESTEUERUNGSABKOMMEN

— Fin. Min. NRW, Erlaß vom 30.11.1966. S 1301-1-VB 1 —

I. Vorlaufige Veranlagungen für 1965 auf Grund zu erwartender Doppelbesteuerungsabkommen

Das Doppelbesteuerungsabkommen mit GRIECHENLAND vom 18. April 1966, das z. Z. den deutschen gesetzgebenden Körperschaften vorliegt,[1]) wird nach seinem Inkrafttreten bereits vom Veranlagungszeitraum 1964 an und das am 23. November 1965 paraphierte Doppelbesteuerungsabkommen mit der SÜD-AFRIKANISCHEN REPUBLIK vom Veranlagungszeitraum 1965 an anzuwenden sein. Der FinMin bittet, die Finanzämter anzuweisen, die Veranlagung für 1965 von

a) unbeschränkt Steuerpflichtigen, die im Veranlagungszeitraum 1965 Einkünfte aus den angeführten Staaten bezogen haben, und
b) beschränkt Steuerpflichtigen, die in einem der angeführten Staaten ansässig sind und denen im Veranlagungszeitraum 1965 inländische Einkünfte zugeflossen sind,

vorläufig durchzuführen oder bis zum Inkrafttreten dieser Abkommen zurückzustellen. Entsprechend ist bei Steuerpflichtigen, bei denen das neue Doppelbesteuerungsabkommen mit Griechenland anzuwenden sein wird, hinsichtlich der noch offenen Veranlagungen für 1964 zu verfahren.

Die Ratifikationsurkunden zum neuen DEUTSCH-ENGLISCHEN DOPPELBESTEUERUNGSABKOMMEN vom 26. November 1964 werden voraussichtlich in Kürze ausgetauscht[2]) das Abkommen wird mit Wirkung vom Veranlagungszeitraum 1960 an anzuwenden sein. Soweit Veranlagungen, bei denen dieses Abkommen von Bedeutung ist, vorläufig sind, können sie nach dem Inkrafttreten des Abkommens endgültig durchgeführt werden, wobei für die Jahre ab 1960 die Übergangsregelung des Artikels XXIII Abs. 4 des Abkommens zu beachten ist.

Die Ratifikationsurkunden zum Abkommen mit ISRAEL vom 9. Juli 1962 sind am 21. Juli 1966 ausgetauscht worden. Soweit Steuern früherer Veranlagungszeiträume mit Rücksicht auf dieses Abkommen nur vorläufig festgesetzt worden sind, können sie nunmehr endgültig veranlagt werden.

II. Stand der Doppelbesteuerungsabkommen und der Doppelbesteuerungsverhandlungen

ARGENTINIEN

Das Abkommen vom 13. Juli 1966 liegt z. Z. den gesetzgebenden Körperschaften vor (Bundestagsdrucks. Nr. V/1087). Das Abkommen wird nicht rückwirkend anzuwenden sein.[3])

BELGIEN

Der Abkommenstext ist am 3. Februar 1966 paraphiert worden. Das Abkommen soll bereits ab 1966 anzuwenden sein.

SOUTH AMERICAN STATES CONCLUDING TAX TREATIES

One of the most remarkable recent developments in international tax law is the number of South American States concluding tax treaties. We mention the treaties concluded by:
Brazil with Sweden of September 17, 1965; Peru with Sweden of September 17, 1966;
Brazil with Japan of October 28, 1966; Argentina with Germany of July 13, 1966.
Negotiations have also started, for example between Brazil and Germany and with the U.S.A. Discussions are also to be initiated by a number of other countries.
The subject of the Supplement to this issue of the Bulletin is the treaty concluded between Argentina and Germany. In this important treaty, the exemption method—with progression reservation—as well as the credit method, has been used by Germany. By using the credit method, Germany grants a fictitious credit to eliminate the possibility of German taxpayers not being able to benefit from the special concessions granted by Argentina. Thus the credit method is applied not only in cases where double taxation exists, but is used as an economic measure in order to promote German investments in Argentina.

BRASILIEN
Im Jahr 1966 sind die Verhandlungen über den Abschluß eines Doppelbesteuerungsabkommens aufgenommen worden.

GRIECHENLAND
Siehe Abschnitt I.

GROSSBRITANNIEN
Siehe Abschnitt I.

IRAN
Im Jahr 1966 sind die Verhandlungen über den Abschluß eines Doppelbesteuerungsabkommens aufgenommen worden[4]).

ISRAEL
Siehe Abschnitt I.

ITALIEN
Die im Jahr 1963 aufgenommenen Verhandlungen über die Revision des bestehenden Doppelbesteuerungsabkommens vom 31. Oktober 1925 sind auch im Jahr 1966 nicht weitergeführt worden.

JAPAN
Das Abkommen vom 22. April 1966 liegt z. Z. den gesetzgebenden Körperschaften vor (Bundestagsdrucks. Nr. V/1045). Das Abkommen wird nicht rückwirkend anzuwenden sein.[5])

KANADA
Die im Jahr 1961 aufgenommenen Verhandlungen über die Revision des bestehenden Doppelbesteuerungsabkommens vom 4. Juni 1956 sind auch im Jahr 1966 nicht weitergeführt worden.

KOLOMBIEN
Das Abkommen vom 10. September 1965, das sich auf die Vermeidung der Doppelbesteuerung der Schiffahrt- und der Luftfahrtunternehmen auf dem Gebiete der Steuern vom Einkommen und vom Vermögen beschränkt, ist von den gesetzgebenden Körperschaften verabschiedet worden (Bundestagsdrucks. Nr. V/331).[6]) Das Abkommen wird bereits am 1. Januar 1962 an anzuwenden sein.

MALAYSIA
Die Verhandlungen über das Doppelbesteuerungsabkommen sind praktisch abgeschlossen, jedoch konnte der Abkommenstext noch nicht paraphiert werden.

PAKISTAN
Das am 27. August 1963 unterzeichnete Zusatzprotokoll zum Abkommen vom 7. August 1958 konnte auch im Jahr 1966 noch nicht den gesetzgebenden Körperschaften vorgelegt werden.

PORTUGAL
Am 4. November 1966 ist der Entwurf eines Doppelbesteuerungsabkommens paraphiert worden. Das Abkommen wird grundsätzlich nicht rückwirkend anzuwenden sein. Für die Schiffahrt- und Luftfahrtunternehmen soll es aber bereits vom 1. Januar 1963 an gelten. Sobald der deutsche Text verfügbar ist, wird der FinMin ihn übersenden.

SCHWEIZ
Die im Jahr 1965 aufgenommenen Verhandlungen über die Revision des bestehenden Abkommens vom 15. Juli 1931/20. März 1959 sind im Jahr 1966 zwar fortgesetzt worden, konnten jedoch nicht abgeschlossen werden.

SPANIEN
Der am 29. Mai 1966 paraphierte Text eines Abkommens konnte noch nicht unterzeichnet werden.[7]) Das Abkommen wird grundsätzlich rückwirkend anzuwenden sein. Es soll jedoch für die Luft- und Schiffahrtsunternehmen bereits ab 1961 gelten.

SÜDAFRIKANISCHE REPUBLIK
Siehe Abschnitt I.

THAILAND
Der am 14. April 1965 paraphierte Text eines Abkommens konnte noch nicht unterzeichnet werden. Das Abkommen soll ab 1966 anzuwenden sein.

NOTEN DER SCHRIFTLEISTUNG

1) Nummehr von Bundestag und Bundesrat zugestimmt; Bundesgesetzblatt II, 25. Februar 1967, S. 852 ff.
2) 30. Dezember 1966.
3) Nunmehr von Bundestag und Bundesrat zugestimmt; Bundesgesetzblatt II. 25. Februar 1967, S. 837 ff.
4) Paraphierung am 24.11.1966.
5) Nunmehr von Bundestag und Bundesrat zugestimmt; Bundesgesetzblatt II, 25. Februar 1967, S. 871 ff.
6) Zustimmungsgesetz vom 2. Februar 1967, Bundesgesetzblatt II, 10. Februar 1967, S. 762.
7) Unterzeichnet am 5. Dezember 1966.

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EDITORIAL:

NEUTRALITY, SOCIAL POLICY, THE TVA AND SALES TAXATION AT THE RETAIL LEVEL

With a view to achieving a measure of neutrality in the impact of the sales tax, the Canadian Royal Commission on Taxation, in its recent Report, recommends that the existing federal sales tax at the manufacturing level should be replaced by a federal sales tax to be applied at the retail level on both consumer goods and services. In this connection, the Commission states that only at this tax level can neutrality be achieved without sacrificing simplicity or that simplicity can be achieved without sacrificing neutrality. The motives behind the proposal are summarized in this issue beginning at page 179.

The Royal Commission did not propose the adoption of a tax on value added (TVA). With the goal of neutrality in mind, the recommendation of a TVA structure would not have been an unusual one. Canada, already experienced with provincial sales taxation at the retail stage, is probably not overly concerned with tax evasion at this level and apparently does not foresee difficulties in differentiating between an entrepreneur's turnover in taxable consumer goods and services and in non-taxable producer goods and services. Moreover, the Commission has suggested specific exemptions to prevent "regression". This social aspect could also be attained under a TVA system, though in a somewhat more complex way. In order to exempt specific consumer goods from a TVA, the necessary collecting, crediting and refunding of the tax at stages previous to the consumption stage can be quite cumbersome. From a fiscal point of view, what with the work involved and no tax revenue resulting therefrom, this is not an attractive alternative.

We feel that the TVA is not the best fiscal structure in terms of social policy. From the point of view of neutrality, a TVA and a sales tax at the retail level can, in principle, be identical. This may be a drawback of a TVA, its ideal function being that of a revenue producer. Political aims should be fulfilled by other more suitable means. Our complex society requires now, more than ever, a rational tax system. Aware of the restrictions of a TVA, the Canadian proposal could be a major step toward such a system.

DR. J.C.L. HUISKAMP

* * * * ARTICLES * * * *

H.W.T. PEPPER:

TAXATION OF BETTERMENT AND CAPITAL GAINS

with special reference to developing countries

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INTRODUCTION

The formal taxation of capital gains[1]) is still a somewhat controversial subject and it would be fair to say that there is not yet a settled consensus of expert opinion on a number of important policy aspects. The viability of such a tax in developing countries generally has by no means been fully borne out in practice. In an environment where investment risks tend in general to be higher, it is generally expected by investors that opportunities for profit including capital gains should also be higher. A tax

[1]) See p. 152, footnote 1.

which takes some of the profit out of those gains reduces the attraction of investment.

2. Full-scale capital gains taxation[1]) involves lengthy and highly sophisticated legislation and provokes considerable avoidance as well as evasion activity. Yields from the tax are notoriously low even in industrialised countries. (See paragraph 42).

3. There is an unanswerable case in terms of social justice for formal capital gains taxation but the case is not so clear in economic terms.[2]) Moreover unless a tax can be made effective administratively so as to produce a worthwhile yield in annequitable manner, and in such a way as to be neutral in its impact between different types of economic endeavour, it may be unacceptable as a means of raising revenue even if it is sound in theory.

4. It is not yet fully clear that a formal capital gains tax can be made to satisfy the tests in the previous paragraphs even in developed countries. Application of the tax to developing countries is therefore of even more dubious validity particularly if it were proposed to introduce a full-scale capital gains tax in a single stage.

5. Apart from problems of administration which include rapid recruitment of additional staff of high calibre there is what may be called the "geographical" enforcement problem. The latter consists of the difficulty of taxing foreign transactions by residents of the taxing country and local transactions of nonresidents.

Grappling with this particular problem may have disproportionate adverse balance of payments effects as residents seek to place more of their capital transactions beyond the reach of the tax and, as noted above, foreigners are to some extent dissuaded from investment.

6. While a formal capital gains tax is a formidable administrative proposition, there are however various other simpler ways of taxing capital gains. Consideration of these is given in the following notes both as an alternative to and in appropriate cases as a stage in development towards a full-scale capital gains tax. Both from the point of view of administration and with the object of minimising economic repercussions it is desirable when the introduction of capital gains taxation is decided upon, to proceed in easy stages.

GENERAL

7. Policy-makers have to bear in mind that—

(a) capital gains taxation has never been notable for yielding a sizeable revenue (see para. 40);

(b) factors (such as a gains tax) which tend to restrict the free movement of the markets in stocks and shares and real property may have disproportionately large effects on the economy;

and thus usually weigh up (a) and (b) against social and other factors in determining fiscal and economic policy with regard to this type of tax.

8. Because of the obvious political implications of a tax which seeks tribute from the rich man's capital gains to counter-balance the income taxes on the "poor" man's wages it is inevitable that capital gains tax should have been tried in a large number of countries—with mixed results and sometimes

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1) The expressions "formal" or "full-scale capital gains tax" are used to refer to the comprehensive taxation of capital gains as, e.g. in the U.S.A. and in distinction from the partial or quasi gains taxes referred to in paragraphs 9 et seq.

2) See, e.g. footnotes to paragraph 8.

in a rather "on-off" manner[3]) with switches coinciding with changes in the political or economic scene. Before discussing formal capital gains taxes a brief reference to what might be called embryo capital gains taxation may be useful.

OTHER TAXES ON CAPITAL GAINS

LAND CONVERSION OR "BETTERMENT" CHARGES

9. When a person who has acquired land for agricultural use receives authority to convert the land to other uses—e.g. for urban development or for mining—it is customary in some cases for the state to make a charge for granting permission for the change. This conversion fee could be regarded as a simple form of capital gains tax, the capital gain resulting from the conversion of the land from one type of use to another, more lucrative, use.

Britain

10. In some cases, instead of a conversion fee, there is levied a tax or "betterment charge". One example was provided by the United Kingdom development charges levied under the Town and Country Planning Act of 1947 which were 100% of the increase in the value of the land attributable to the granting of planning permission, e.g., for the conversion of agricultural land to housing sites. These charges produced a net yield of about £17,000,000 in the period 1948-1952. The Development Charges were repealed in 1952. The British Land Commission White Paper Cmd. 2771 published in September, 1965 and now incorporated in a Bill proposes however to revive such charges which will be made initially at the rate of 40% on the increase in value. The present proposal is regarded as much more viable than the earlier levy which by taking all the profit out of development slowed that process down.

---

3) 1. *India* Capital gains were taxable in the years 1946/7 and 1947/8 and the tax was then abolished because of the dampening effect on the property market and because of agitation against high taxes generally.
The tax was re-introduced in 1957/8 and substantially modified in 1963. The yield from the taxation of capital gains in tax year 1961/2 was Rs.14m. (on taxable gains of Rs.63m.) compared with a yield of approaching Rs. 4,000m. from income tax; in percentages terms the capital gains tax yield was about 0.4% of income tax for that year.
2. *Israel* Capital gains tax introduced 1 April 1965 at the rate of 25% with graduated time abatements for assets held over 1 year and, with exemption for those held over 18 years. The tax was withdrawn as regards gains on stocks and shares in July, 1965.
3. *Japan* Capital gains were made taxable in 1950 on advice of the Carl S.Shoup Commission. Capital gains tax on stocks and shares was repealed 1953 because the tax hampered development of the securities market and was difficult to collect.
4. *Pakistan* Capital gains tax operated from 1946 to 1949 and was then suspended because it discouraged the capital formation which was especially needed after the disorganisation following the partition of India and Pakistan. The tax was revived in 1963 with a basic exemption of Rs.10,000 for individuals and a tax rate of 20% on companies.
5. *Malaysia and Singapore* Capital gains tax was announced in November, 1964 in the Malaysian federal budget of 1965. It was withdrawn by the Peoples' Action Party Government of Singapore on that country's separation from Malaysia in August, 1965, and by the Malaysia Government shortly afterwards.
6. *Holland* A proposal for a capital gains tax during 1966 was withdrawn for further consideration.

Malaysia and Singapore

11. Three of the states of Malaysia (Selangor, Negri Sembilan, and Pahang) have introduced conversion fees which are payable when permission is given to develop land. The rate of "tax', or fee charged, is 20% in Selangor and Pahang and 25% in Negri Sembilan. The system has been highly productive in Selangor where considerable development has taken place in recent years, the yield being in the neighbourhood of $5,000,000 in each of 1964 and 1965. The 20% levy was made on the difference between the value of the land after development permission, and its agricultural value. In Pahang, where the levy was imposed in 1964, collection was sluggish because of opposition on the grounds that the charge would slow down development. In Singapore a law was passed in 1964 to enable the government to impose development charges when permission was given to develop a residential area to a density in excess of the average or in a manner different from that laid down in the Master Development Plan.

Jamaica

12. Another type of scheme was promulgated in Jamaica by the Land Development Duty Law of 1958. In respect of certain areas of land, capital gains duty of 25% was to be levied if the land was sold at a profit and a betterment charge of 25% was to be made in respect of land still retained where a periodical re-valuation showed an increase over the corresponding value at a base date. The first re-valuation was made in 1964 and the results in terms of tax yield from the first quinquennial valuation are awaited with considerable interest. During the first 5 years to 1964 there were 102 disposals in the limited area covered by the law producing *realised* gains exceeding £80,000 and tax of £22,000.

13. The specific justification for this tax in Jamaica was that the increase in the value of the land in question was largely attributable to the development expenditures of the Jamaica government and the tax was restricted geographically to the area which benefitted.

DEVELOPMENT CHARGES FOR REIMBURSEMENT OF GOVERNMENT EXPENDITURE

14. Where government expenditure, for example, on building access and feeder roads is entirely specific, it is common for the costs to be parcelled out and charged to the holders of the frontages bordering the road either ad hoc or by means of "road charges", "rates" or other local government levies. Where the benefit is not quite so specific, for example, in the case of an area drainage or irrigation scheme it is not unusual for the maintenance and amortisation costs to be charged to the holders of the land in the benefited area (see example in paragraph 19).

15. In the examples in paragraph 14, the justification for the charge is plain—the value of the land has been increased by the services provided and government is recouping its expenditure more or less specifically.

16. The charges quoted in paras 9-12 were not computed precisely to recoup the relevant proportions of government expenditure incurred[4]) and thus the charges

4) Of course the rationale of the tax is that the increase in land values is largely attributable to Government expenditure generally on opening up land, providing trunk raids and other facilities.

made were nearer to capital gains tax proper.
17. In a somewhat "in-between" category are the charges or "reserves" levied in New Zealand by virtue of which a property developer was required to hand over a percentage, for example 10%, of the total areas to be developed to the local authority. The area handed over would be for use as parks, playgrounds etc. Where development was in a city area, the area to be handed over might be too small for effective public use and a cash levy in terms of a percentage of the total selling price was made instead—here again the embryo of a capital gains tax may be observed.
18. A similar policy was applied in New Zealand to buildings built in town centres. For every 1,000 sq.ft. of floor space, 200 sq.ft. of car parking space had to be provided.[6]) Something similar has been adopted in other places e.g. Chicago, U.S.A., but the tendency usually is for conversion of the "space" requirement into cash terms.

IMPROVEMENT TAXES

19. Another type of betterment charge is that levied on improvements to land made by a government, for example, by a drainage and/or irrigation scheme covering a large area. Clearly the owners and occupiers of the land in question will directly benefit from the scheme and the cost should as far as possible be charged to them rather than to the nation as a whole. Such charges are not always easy to levy and collect. When made, they are usually levied as an annual charge on the improved land in order to service, or partly to service, the debt capital used to finance the improvement scheme. Obviously there would be a case for a charge on the capital value of the improvement to be levied on the owners of the land on the lines of the British or Jamaican betterment charges. Such a charge would, however, be difficult to collect because the small owner's immediately cash resources would not be increased by the fact that his land had increased in value.
20. A typical betterment scheme of this kind is that covered by the Pakistan Betterment Tax Ordinance No. III of 1964 which relates to the Ghulam Mohammed Barrage Canals irrigation scheme.
21. Annual charges made are proportional to the benefits likely to be received under the irrigation scheme but cannot be regarded as amounting to the taxation of capital gains.

"Once-for-all" taxes

22. A tax somewhat akin to capital gains taxation though with some important differences was levied in Norway after the Second World War. Taxpayers were charged on the increase in their capital as at September 1945 over the capital in 1940 at rates ranging from 20% to 80% after deducting a basic exemption. The increase in capital was of course attributable partly to savings but these would presumably not have been large during the German occupation and the main targets were the capital gains and the accumulations of wealth made through profiteering and black-marketing during that period.
23. An important factor in the success of this tax (which produced a yield of K495,000,000) was that popular feeling was very strongly against war profiteers. The administrative

---

5) Another example of planning permission being tied to the provision of public car parking facilities by the developer has recently (February, 1966) given rise to a Parliamentary Question in Britain. Certain local authorities including those for Bridgewater and Dunstable had been taking an initiative in this respect.

basis was also sound since the Norwegian capital tax structure was well established and provided the datum capital figures for 1940 with which the 1945 comparison was made.

24. A tax recently proposed in Sweden which is intended to fall on developments in the shape of certain types of new buildings is referred to in paragraphs 32-34.

STAMP DUTIES AND TRANSFER TAXES

INTRODUCTION

25. Because the transfer of ownership of real property has from time immemorial been documented and recorded such transfers have also commonly been made the subject of taxation. The value of real property has increased fairly steadily over the centuries so that transfers of ownership have generally involved the realisation of a capital gain. Stamp duties, (sometimes referred to as transfer taxes), in the form of an ad valorem tax on the sale price are not of course a capital gains tax in the proper sense of the word. To the extent, however, that stamp duty cannot be shifted forward, it effectively appropriates part of the gain on transfer of ownership for the national revenue.

26. The tax is of course a crude one as far as capital gains are concerned because the same amount is payable whether the property is sold at a lage profit, at a small profit, or even at a loss. Nevertheless because real property values are generally rising the broad impact of the tax will not be inequitable. High rates of tax on real property sales are levied, for example, in Belgium, France, Germany, Greece, and Portugal; the first of these countries having recently raised its tax rates substantially[6]).

AVOIDANCE AND EVASION OF DUTY

27. Both avoidance and evasion are practised with regard to stamp duties. Evasion is achieved either by not disclosing the transaction or by understating the price at which the property changed hands. Underdeclaration may suit both buyer and seller, the buyer because, if he has been evading tax, the smaller the purchase price purports to be the smaller sum of money for which he may have to account. In the case of the seller a fictitious sale price lower than the actual price will minimise any capital gains tax he might have to pay in the profit from realisation. Avoidance may be accomplised in the case of a graduated stamp duty by disposing of an asset piecemeal so that the lowest rate of tax applies repeatedly to different parts of what is basically the same transaction. Because stamp duties are normally levied on a particular form of transfer, avoidance may be practised by making the transfer in a different, untaxed, form.

GRADUATION OF STAMP DUTY

28. It is not uncommon for an enlightened government to use fiscal and other methods to encourage ownership of residential property by the lower income group to produce a property-owning democracy. In

6) The Belgian rate is 11% on sales up to B.Fr. 1,000,000 (= US$20,000) and will now increase to a maximum of 14% on sales exceeding B.Fr. 5,000,000 (= U.S. $100,000). In France, the duty is 16.6% on land, buildings and goodwill while the rate is higher on building land if the building is not completed by a certain date. Germany has a duty of 7%, Portugal a transfer tax at a basic rate of 8%, and Greece a 9% transfer tax.

this context it would hardly be appropriate to charge full stamp duty on the purchase of low-costing housing[7]). On the other hand, houses in the higher price ranges can clearly bear material amounts of stamp duty. It is thus desirable to have a scale of rates on real property starting with NIL below a certain level (but only where the property can be classed as low-cost housing for a family unit) but with rates which increase above that level.

MEASURES TO COUNTER AVOIDANCE AND EVASION

29. When a scale of stamp duty rates applies, the device of selling large assets by a series of small transactions (e.g. an office block might be sold office by office or room by room) to take undue advantage is usually countered by provisions to the effect that a series of transactions which are in substance a single transaction should be aggregated for the purpose of calculating the duty.

30. Evasion by underdeclaration, which is prevalent in most countries, may be countered by checking procedures. The fee charged by a lawyer for making a legal conveyance is often proportional to the sale price of the property and so is the fee charged by an estate agent. The property itself or similar neighbouring properties may have been previously sold, or valued for death duty or compensation purposes. There may therefore exist information on professional fees or property values which provides a useful comparison for checking purposes.

DEVELOPMENT INTO CAPITAL GAINS TAX

31. It is clear that practical experience of administering and properly enforcing a graduated stamp duty would be a useful preliminary to the enactment of a full-fledged capital gains tax. If stamp duty cannot be properly enforced, it is inconceivable that capital gains taxation could be equitably levied and the latter should not therefore be contemplated before experience has been gained by making stamp duty viable.

TAXES ON NEW BUILDINGS

32. An example of a tax on new buildings, which is likely to fall at least partly on the capital gain which results from the development involved, is provided by the new tax announced in the Swedish Budget on 11th January, 1967.

33. One item in a deflationary Budget is a 25% levy on the total construction cost of "non-essential" buildings, including offices, banks, shops, assembly rooms, petrol stations and sports' stadiums. The tax is equivalent to a once-for-all stamp duty at an unusually high level and like some other stamp duties is selective in favouring housing, which is not taxed at all. The bias against non-industrial buildings is parallel to that found in the tax depreciation laws of many countries which provide tax relief for industrial buildings but none for shops, office blocks etc.

34. It may be noted however that hotels are not included in the list of "non-essential" buildings—this reflects the growing favour

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7) For example in Britain, there is exemption and graduation in the stamp duty on property conveyance as follows:-

Stamp Duty on Conveyance of Property

Value	Duty
Up to £4,500	NIL
Up to £6,000	5/- per £50 (= ½%)
Exceeding £6,000	10/- per £50 (= 1%)

(There is also exemption in Britain from purchase tax for residential caravans and their fittings.)

with which both industrial and developing countries nowadays look upon the tourist industry and the fixed capital employed therein.

CORPORATE DISTRIBUTIONS INCLUDING TERMINAL DISTRIBUTIONS

35. Where capital gains are made by companies the gains may find their way to shareholders either—

(a) by way of the annual distributions of income (and sometimes capital) made by companies; or
(b) in the terminal distributions to shareholders made when a company liquidates or winds up.

36. It is a relatively simple matter to provide that all distributions by companies to their shareholders should be regarded as income in their hands for income tax purposes and this is an effective way of taxing distributed corporate taxable gains where no formal capital gains tax exists. It is of course necessary, in order to prevent a simple tax avoidance device, to deal with the reduction and repayment of capital to shareholders where this is accompanied by bonus issues or stock dividends to restore the capital, by deeming such operations to constitute distributions. A genuine reduction and repayment of subscribed capital when a company reduces its activities does not of course qualify as a taxable distribution..

37. Such provisions regarding terminal distributions are a fairly usual anti-avoidance device in countries[8]) where shareholders are taxed on dividends received in addition to the tax charged on the corporate income out of which the dividends are paid. It may however be necessary to extend the legislation slighly in order to cover the capital gains as well as the income of companies.

TRANSITION TO A FORMAL CAPITAL GAINS TAX

38. A country which has adopted some or all of the types of taxation referred to above will have covered many of the sources of capital gains and there will probably be little revenue potential in what remains of the field for such tax. A developing country would be well-advised to take further steps towards more comprehensive gains taxation only after careful deliberation.

39. There is in fact a good deal to be said, if full capital gains taxation is to be developed, for the view that the tax would be introduced in easy and graduated stages, commencing at low rates and initially covering only certain types of assets. Land and real estate generally are probably the best candidates for the initial scope of the tax leaving shares and other assets to be included later.

40. The introduction of a formal capital gains tax proper does not necessarily imply the abolition of the other types of levy referred to, although e.g. stamp duties on real estate transfers might be reduced when the actual gains become taxable. Since, however, capital gains tax is normally levied only on realised gains, there would be a good case for retaining betterment or development charges which are payable when the increase in value takes place, making an offset, in appropriate cases, against the capital gains tax payable where realisation takes place soon after a betterment charge has been paid.[9])

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8) Such provisions exist in many countries e.g. Sweden, United Kingdom, U.S.A., and India (see section 2(22), I.T.A. 1961).

9) Where realisation takes place a considerable time (say more than 1 year) after betterment charges have been paid the latter should be regarded as an expense reducing the realised gain.

CAPITAL GAINS TAX

PROS AND CONS OF CAPITAL GAINS TAX

41. In favour of capital gains taxation it is argued—

(i) there is no equity in a situation where one section of the community makes untaxed capital gains which can be used as income while other taxpayers are fully taxed on ordinary income;

(ii) however much capital gains may be discounted as "paper" gains resulting from currency devaluation and other factors, the recipient is demonstrably better off than the taxpayer without such gains, and whose savings may be in fixed deposits or fixed interest stocks. The taxpayers making such gains should therefore pay more tax than those who do not;

(iii) if capital gains are taxable, it is easier administratively to deal with income tax evaders who might otherwise avoid penalty by ascribing unexplained accretions of wealth to non-accountable capital gains.

42. The following arguments are made against capital gains tax—

(i) a capital gain may represent an increase in value over a very long period; it is not equitable to tax it as an incoming of the year of realisation;

(ii) such a gain may be a once-in-a-lifetime (taxed) gain which may be followed in later years by (unrelieved) capital losses so that the taxpayer has no net life-time gain but has nevertheless paid tax;

(iii) some gains are illusory being merely a reflection of currency depreciation and not a gain in real terms; "gains" from fixed interest securities merely reflect a fall in the rate of interest;

(iv) a gains tax on lands tends to increase the price of land and the difficulties of acquiring land for development;

(v) a gains tax on shares tends to inhibit "stagging" and other necessary operations and to encourage transactions outside the stock market which evade stamp duty;

(vi) Not to allow capital losses as a deduction against income is inequitable; to do so may put income tax revenue in jeopardy in times of stock market depression;

(vii) some capital gains, arising, for example, from compulsory purchase, are unsought, unwelcome, and may result in real losses from disruption of business outweighing any superficial gain;

(viii) capital gains taxation discourages investment in equities and growth enterprises generally and is particularly unsuitable for developing countries;

(ix) capital gains are not solely the preserve of the rich—the "poor" can obtain capital gains through holdings in unit trusts;

(x) the yield of capital gains tax is low,[10]) and quite incommensurate with the economic harm which the tax might do;

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10) e.g. In the U.S.A., which has had over 50 years' experience of capital gains taxation, declared capital gains have for some years past been rather than 2% of declared income for income tax and the capital gains tax rate is about half the income tax rate. In India capital gains tax in 1961/2 yielded about 0.4% of the income tax. In the U.K. the shortterm gains tax yielded about £1½ million in 1963/4; £3 millions in 1964/5; and £3½ millions in 1965. The new capital gains tax produced £2.4 million in the

(xi) because gains which accrue within the taxing country are more likely to be effectively taxed than those realised abroad, there is an incentive to taxpayers to invest abroad and hope to escape capital gains taxation at home. This is likely to be harmful to the balance of payments and to the development of the country in general;

(xii) capital gains taxation may encourage monopolies because some of the attraction of investment in new risky enterprise (the possibility of untaxed capital gains) is removed and investment in larger, older and less-enterprising concerns providing steadier income and smaller growth prospects is then more favoured.

CAPITAL GAINS TAXATION: GENERAL POLICY

43. The following paragraphs deal with various important points of policy which require to be considered from the aspects of administrative feasibility, equity, and the prevention of tax avoidance.

SCOPE OF TAXABLE GAINS

44. It has already been suggested that capital gains tax should be developed in stages, the logical choice for the first step being land and real property which, as noted earlier, may already be subject to something akin to capital gains tax. Other points concerning the scope of the tax are discussed below.

EXEMPTION LIMIT

45. When first introducing capital gains taxation, it is desirable to have a fairly high exemption limit so that small gains are not liable to tax and what would otherwise be a formidable administrative problem can be minimised. Where capital gains taxation is an entirely separate tax from income tax, the case for an exemption limit is overwhelming. Without it, persons[11]) below the income tax limit would be paying capital gains tax on gains realised e.g. from the sale of quite tiny pieces of land and this would be a somewhat ridiculous state of affairs. An exemption limit is for example provided in Pakistan where in effect gains of less than Rs.10,000[12]) are exempted, while gains above Rs.10,000 are abated before applying tax.

46. Where capital gains tax is integrated with income taxation, the position is of course different because the exemptions and reliefs under the income tax code would apply to both income and capital gains.

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period 6th April to November, 1966 and is estimated to produce £5 million in the year to 5th April, 1967 compared with a total of £5,003 from all income taxes and £10,234 total revenue. This last comparison however is hardly meaningful in view of special circumstances such as the newness of the tax and the deflationary policy of the U.K. Government which limited the scope for realising capital gains in the relevant period. The £5 million estimate for 1966/67 compares with an estimate of £75 million for stamp duties indicating that the latter can by no means be "written off" as a source of revenue in modern conditions.

11) Such persons would include peasants in countries where the inheritance laws, and a high birthrate, result in land holdings being reduced after a few generations to "pocket handkerchief" proportions.

12) Exemption limits in other countries include the following:

Argentine	Pesos	100,000	
Austria	Sch.	40,000	
Burma	Kayats	25,000	
Ceylon	Rs.	2,000	or Rs. 5,000
Denmark	Kr.	1,000	or Kr. 3,000
Germany	Dm.	10,000	
India	Rs.	5,000	
Indonesia	Rp.	50,000	
Japan	Yen	150,000	

47. With the introduction of capital gains taxation in a developing country there is almost certain to be a serious shortage of high calibre staff to administer the tax. For the sake of simplicity it will be desirable to keep the tax separate from income tax. A high initial exemption limit will keep the number of taxpayers within reasonable bounds and in general restrict liability to the wealthier taxpayer whose tax returns will often be rendered by a professional accountant.

48. Apart from the question of exempting gains below a certain figure, there are certain types of gains which should be considered for exclusion as a class from the scope of capital gains tax. This subject is discussed in the following paragraphs.

EXCLUSION: CHATTELS

49. For administrative reasons and because little revenue potential exists, chattels such as private motor cars, furniture, personal ornaments and jewellery should certainly be excluded from the initial scope of capital gains tax. The matter can always be reconsidere at a later stage, if there appears to be material tax lost through this exclusion. Many countries with established capital gains taxation either exempt or abate the tax where a gain results from disposal of a personal chattel. In Britain exemption is granted where the disposal produces less than £1,000.

EXCLUSION: STOCKS AND SHARES

50. As mentioned in paragraph 39, it may be administratively desirable to restrict capital gains taxation initially to land and other real property (and the various titles thereto) leaving stocks and shares to be tackled later. This leaves a potential loophole in that a company may own real property and instead of selling the property the owner of the company's shares may sell his shareholding realising a gain on shares instead of on property. This loophole is not as wide as may appear at first sight. If the sale is at arm's length the purchase is more likely to want a personal title to the property than to wish to be a party to a tax-avoidance manoeuvre which may boomerang upon him should he wish at a future date to put the property into his own name.

51. At any rate, the risk of avoidance schemes of this kind is the price which has to be paid initially if the administration burden of capital gains tax is to be kept within reasonable bounds. Various countries have in fact approached capital gains taxation in this way (e.g. Argentina, Israel) by excluding stock exchange profits from the initial scope, others have been fairly generous in allowing abatements where the gains were re-invested, and others (e.g. Spain) tax such gains only when realised within a short period (e.g. 12 months in the case of Spain).

EXCLUSION: PRIVATE RESIDENCES

52. It is usual[13]) to exclude from the scope of capital gains tax a profit made on selling a taxpayer's residence. The best method of affording relief is that adopted in the U.S.A. where the capital gain on realisation is computed in the usual way but is then deducted from the cost of the new resi-

13) It has been argued that there is no more justification for exempting residence than any other investment. So long as housing shortages continue however so that tax payers are forced to invest in house purchase merely to keep a roof over their heads it is likely that residences will continue to receive the favourable tax treatment now commonly applied to them.

dence instead of being immediately charged to tax. This effectively and simply prevents tax avoidance, for example, by a taxpayer residing temporarily in a large mansion for the sole purpose of "franking" the subsequent gain from tax. Where the gain on sale is larger than the cost of a subsequently purchased residence, the surplus will be taxable. Where a further sale of residence takes place later, only the cost of the second residence as reduced by the previous gain (or by NIL if the gain exceeded the cost) may be deducted from the selling price. The gain on the second transaction is thus enhanced by the gain on the first. If a series of transactions is undertaken, the effect is cumulative so that even though each residence is replaced, a taxable gain eventuates as soon as the cumulative gain exceeds the cost price of the new residence. (See example in paragraph 53). By this time the taxpayer has realised a tax-free capital gain equivalent to the cost of his latest residence and thus has been reasonably generously treated.

53. The following example illustrates the exemption referred to in paragraph 52.

Year 1	Residence No. 1 purchased for		£3,000
Year 4	Residence No. 1 sold for £3,600		
	Residence No. 2 bought for	£4,000	
	Capital gain on Residence No. 1 = £3,600−£3,000 = £666		
	Offset capital gain from cost of Residence No. 2.	£ 600	
	Revised basic cost of Residence No. 2.	£3,400	
Year 7	Residence No. 2. sold for £5,000		
	Residence No. 3 bought for	£6,000	
	Capital gain on residence No. 2		
	sale price	= £5,000	
	deduct revised basic cost	£3,400	
	Capital gain	£1,600	
	Offset Capital gain against Residence No. 3.		£1,600
	Revised basic cost of Residence No. 3.		£4,400
Year 15	Residence No. 3. sold for £10,000		
	Residence No. 4. bought for (taxpayer moved to less expensive part of country)		£5,500
	Capital gain on residence No. 3.		
	sale price	= £10,000	
	deduct revised basic cost	= £ 4,400	
	Capital gain	£ 5,600	
	Offset some of Capital Gain	£ 5,500	
	Capital gain	£ 100	£5,500
	Chargeable		
	Revised basic cost of Residence No. 4.		NIL

Note 1: When Residence No. 4. is sold the whole of the proceeds (less expenses, see Note 2) will represent a capital gain but this can in turn still be offset against the cost of Residence No. 5.

Note 2: In order to keep the above example fairly simple all expenses have been omitted. In practice a capital gain on the sale of property would be reduced by—

(a) the cost of improvements done between purchase and sale; and
(b) the cost of selling, including advertising, agents' commission, and legal fees.

Note 3: It will be noted that the effect of the offset provisions is that increasing amounts of latent capital gains liability are accumulated (in the example, £600, £1,600, and £5,500) but that the liability to tax thereon may be postponed almost indefinitely.

54. A simpler method is to exclude altogether from tax the capital gain on a taxpayer's principal residence and in introducing a new capital gains tax it is preferable to begin with a provision of this kind. At a later stage it will be necessary to elaborate the provisions in order to cope with avoidance, e.g., by means of a series of realisations of residences successively bought and sold by the same person. This may be done simply by limiting tax exemption to one transaction per taxpayer but this restriction will not in general work out so fairly as the system referred to in paragraph 52 mainly because there will be a lack of parity between different taxpayers.

55. For example a taxpayer, whose employment involves him in periodical transfers from one town to another and hence in a series of property transactions, is worse off under a "single life-time exemption" system than a taxpayer having a more settled employment, business, or profession. Moreover a taxpayer may realise a small tax-free capital gain on a residence and later, having used up his single exemption, become liable to tax on a much larger profit.

56. Other methods of preventing avoidance involve fixing a minimum period of residence before the exemption operates, or endeavouring to decide whether a particular change of residence is done with a view to gain or to some "non-tax" reason such as health or aesthetic choice. The snags, however, are obvious.

Partial Exemption of Residence: Change of Use.

57. A simple and equitable system of giving partial exemption in a case where a house was used for a commercial purpose (e.g. letting to a tenant) by the taxpayer either before or after the period of his residence has been adopted in the British capital gains tax legislation introduced in 1965. To illustrate, assume that the property was held by the taxpayer for a total period of 6 years but was occupied only for 4 years (e.g. either (a) there was 2 years initial letting to a tenant on a lease taken over from the previous owner, or (b) during the last two years of ownership the property was let furnished while the taxpayer waited for a satisfactory sale price). Assuming also that the whole 6 year period has run since the capital gains tax has been introduced the capital gains tax liability would be restricted to

$$\frac{\text{Period of commercial ownership}}{\text{Total period of ownership}} = \frac{2}{6} \text{ x capital gain}$$

Any period when a residence was empty prior to occupancy by the owner or in the time between vacation by the owner prior to selling and the actual sale date would of course be counted as residential (exempt) ownership.

58. *:divided use*

Where a property is used partly for business and partly for residence (e.g. a block of 3 flats or apartments of which the taxpayer-owner occupies one) the common sense solution of limiting exemption to the private portion suggests itself. This solution is in practice widely adopted—it is a feature, for example, of the British and U.S. systems.

EXCLUSION: GOVERNMENT SECURITIES

59. Although capital gains may be realised from government securities just as they may be realised on other securities, a country introducing capital gains taxation is well advised to exclude its own securities from the scope of gains tax, at any rate initially. Where such securities are fairly short-term and have been issued at a discount and at moderate interest holders are likely to become emotional if a tax is introduced after they have partriotically subscribed on the basis of a certain redemption yield and now find that yield reduced by capital gains tax.

60. The premium on maturity of gilt-edged securities is normally a factor in the total redemption yield as announced in the issue terms, is discounted in the stockmarket price and should not in any event be regarded as a capital gain to the investor. A logical treatment therefore is to exclude the margin between issue and maturity price from the capital gains calculation and this course has been adopted, for example, in the capital gains tax operated in the U.K. This part of the yield to the investor is normally exempt, in addition, from income tax.

61. In the case of long-term or undated gilt-edged stocks, these are likely to lose value in real terms in the course of time. Although a capital gain may be made by a taxpayer who has bought gilt-edged under par, he may not be satisfied that he has made a capital gain in real terms and here again the emotions aroused may not be worth the net revenue (if any) to be gained. A developing country endeavouring to create a gilt-edged market in its own securities would certainly be well-advised to omit them from the scope of capital gains taxation.

62. It may be noted incidentally that in general and in the long run, except for stocks issued at a discount or redeemable at a premium, there is no "taxable base" (see paragraphs 64 et seq) for gilt-edged securities. Where, the stock is issued at par and is ultimately redeemed at par, whatever may have happened to the price of the stock in between, the aggregate position of all holders of the stock taken together is a net capital loss even in nominal terms because total gains are exactly offset by total losses but are reduced to a net aggregate loss by the brokerage, stamp duties[14]) etc. incurred on the various purchase and sale transactions.

63. Where gilt-edged transactions form part of the business of a financial undertaking, the profit or loss including discounts on issue or redemption premiums, of course ranks as a profit or loss for income tax purposes and capital gains legislation is irrelevant.

EXCLUSION: "GAMBLING" AND SPECULATIVE GAINS: EXISTENCE OF TAXABLE BASE

64. Gambling gains for the purpose of this section should not be taken to include stock market deals because the subject matter of so-called "gambles" on the stock exchange, mainly equity stocks and shares, are "growth" items. The value of such securities in general increases with the passage of time so that over a period of time the net result of all such dealings is a profit, i.e. there is a "taxable base" or basis on which to found a tax, (see, however, paragraphs 59-63 regarding gilt-edged securities). For this reason it is sound, from the aspect of both policy and administration, to bring share disposals into the capital gains net at some stage, preferably a good deal later than the stage at which real property is made subject to the tax.

65. The same does not hold good for straight gambling for money either in games of pure chance, or mixed chance and skill, at gambling clubs, casinos and other places. The total gains cannot exceed the losses so there is no net tax base on which to found taxation. In cases where an establishment is involved the gamblers' aggregate losses will of course exceed their gains by the amount of the "house percentage" i.e. the proportion of the gross turnover appropriated for the administration. The establishment should pay income tax on its profits and the net loss of the punters as a whole, which completes the equation, clearly provides only a negative base for additional tax revenue.

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14) It may be noted, however, that many governments exempt their own securities from stamp or transfer taxes.

66. This leads logically to the exclusion from tax of all gambling or speculation in "barren' fields of activity where there is no natural growth in the subject matter, e.g. the money gambling referred to in the preceding paragraph, horse-race betting and gambling on other sports, and speculation in commodity futures[15]). Where the total winnings are equal to (or less than because of the deduction of overheads) the total losses, the only hope for gleaning revenue is to contrive to assess the winners without allowing loss relief to the losers.

67. The result predicated in paragraph 66 is in fact regularly achieved in practice without undue difficulty and without public outcry because operators in the gambling and speculative fields can be divided readily into two classes which may be loosely termed "professionals" and "amateurs". Still more fortunately for the administration the professionals as a class make profits, while the amateurs as a whole make losses. Moreover, the former, by definition, are carrying on trading or professional activities, to which their profits accrue, while the latter are not engaged in professional or commercial activity[16]).

68. Apart from getting a good bargain as far as profits and losses are concerned, a government can usually obtain a substantial revenue by taxing the gross turnover of betting and lottery enterprises and has the advantage of being able successfully to adopt a moral attitude while doing so!

69. In so far as horse-race betting is concerned the division may be between the "professionals" (i.e. the bookmakers) and the "amateurs" (i.e. the punters). In the long run the former are winners in total and the latter losers. The former make a business of their activities and are chargeable to income tax. The amateurs make in total, substantial losses (made greater by any betting tax that may exist) which provide no foundation for capital gains taxation.

EXCLUSION: COMMODITY FUTURES

70. In the commodity futures market there is the same professional/amateur division. The professionals, (i.e. the dealers, brokers, hedgers, and those who for trade reasons must sell or buy forward their production or requirements for the particular commodity) make profits in total in the long term. The amateurs who in aggregate make losses from isolated gambling transactions, provide no net scope for taxation. This is because in general, over a period total losses and gains in a commodity market should balance because there is not the same "growth" propensity in commodities as in shares. In fact there are sometimes lengthy periods when commodity prices fall rather than rise.

71. The policy should thus be to leave the amateur alone and continue to charge income tax on the professional, who includes not only those persons referred to above whose business comprises or includes dealings in "futures" but the person who systematically "plays" the commodity markets and is taxable[17]) on his profits for income tax purposes. After excluding these categories, there will clearly be only a total net loss

15) Broadly speaking there is no secular growth in commodity values in real terms although there may be increases in money terms. On the contrary improvements in production and extractive methods tend to result in price decreases. The exceptions to this include commodities such as scarce minerals, the world supply of which is becoming exhausted.

16) See, for example, Graham v. Green where a British Judge described a bet as merely "an irrational arrangement".

17) Cooper v. Stubbs, Brash v.C.I.R.

remaining as the amateur's share and no scope for capital gains taxation.

72. Apart from the lack of a firm foundation for capital gains taxation in the case of the "amateur" and others in the "aggregate loss" category referred to above, the administrative cost of trying to cope with such transactions is likely to be heavy. Because such transactions will produce an aggregate loss which may be set against other taxable gains; only a negative revenue is likely to accrue from inclusion of such transactions in the scope of capital gains tax.

GIFTS, BEQUESTS, AND COMPULSORY ACQUISITIONS

GENERAL

73. In general, capital gains tax applies to realised capital gains and realisation is normally by sale of the property involved. The ownership of property may, however, be transferred by means other than voluntary sale by the owner, for example, by gift or bequest. Even in a simple capital gains tax law cognizance must be taken of transfer by gift, otherwise such transfers open a wide field for tax avoidance.

GIFTS

74. There are broadly two ways of dealing with gifts. One method puts the donee in the donor's shoes regarding the asset which has been given to him. In this case, the donee or recipient is regarded as having acquired the property at the price paid by the donor and at the same date that the donor acqually acquired the property. The other method is to deem the gift to be a sale at current market value. A capital "gain" may then accrue to the donor on which he must pay tax. The recipient is, however, regarded as having purchased the property at the valuation price attached to it. This higher value is then deducted from the proceeds of ultimate realisation by the recipient.

75. The valuation method is in general to be preferred since it is likely to produce revenue earlier than the other method. From a practical point of view also it is preferable for the tax computation on the recipient's realisation to deal with the period from date of acquisition to date of disposal, rather than with a period going back an indefinite length to the original acquisition by the donor.

76. Where gift tax is levied in addition to capital gains taxation, it is desirable to consider whether some abatement is necessary so that the same transaction is not fully charged to both taxes. The rationale of gift tax is of course to collect some of the tax which would have been payable as death duty had the transfer taken place by bequest instead of gift. On the other hand, capital gains tax is only concerned with the excess of value at the date of gift compared with the cost of acquisition. The appropriate way of abating the dual taxation would be to deduct the capital gains tax from the gross value when computing the gift tax—the alternative would be to deduct gift tax from the value in computing the capital gain.

BEQUESTS

77. There is little danger of tax avoidance by transfer of property at death (instead of during the taxpayer's lifetime) becoming a serious menace to the revenue because a man only dies once. It would therefore be safe to omit any reference to bequests from the position would then be that no capital gains initial legislation on capital gains tax. The tax became due from the deceased's estate when property passed on death. The beneficiary on the other hand when disposing

of the asset subsequently would be permitted to deduct from the sale price the estate duty valuation of the asset inherited.

78. The more severe treatment for capital gains tax purposes is to deem the bequest to be a disposal at market valuation. Since estate duty and capital gains tax may both apply to the same property, relief from dual taxation or similar lines to that referred to in paragraph 74 will be required.

COMPULSORY ACQUISITIONS

79. Where property is acquired compulsorily by the government or under some statute, for example, by some public utility corporation there is really no alternative to treating the acquisition as a taxable disposal. If exemption from tax was conferred in respect of such transactions, no voluntary sales of land (needed for example for development or rehousing projects) would take place as all owners would have a tax incentive to hold their land until forced to disgorge it by the exercise of compulsory powers by the state or quasi-state agency.

RETROSPECTION

80. An accusation of "retrospective taxation" is sometimes made against new capital gains legislation which would tax gains from the disposal of assets which were acquired before the law came into force. The usual method[18]) of avoiding retrospection is to limit the taxable part of the realised gain to the proportion which can be reckoned to have accrued between the date of the legislation or the cost of previous acquisition whichever was greater. This copes satisfactorily with the unusual case where the asset was worth less on introduction of the tax than it had originally cost.

81. An alternative means of apportionment is provided in the British capital gains tax legislation of 1965. The taxable gain may be taken to be that part of the total gain from pre-enactment acquisitions which is proportionate to the ratio which the period from enactment to disposal bears to the total period of tenure of the asset. This last technique provides a neat solution and works broadly as follows:—

Example Asset acquired 1960 for £10,000 sold 1970 for £20,000. Capital gains tax introduced 1965.

$$\text{Capital gain} - (£20{,}000 - £10{,}000) \times \frac{(1970-1965)}{(1970-1960)}$$

$$\text{i.e. } £10{,}000 \times \frac{5 \text{ years}}{10 \text{ years}} = £5{,}000$$

82. The other method of avoiding retrospection is to apply the new capital gains tax only to transactions where both the acquisition and the disposal took place after the legislation was introduced. The scope of such a tax is obviously very limited because on the date the legislation comes into effect all property will be in someone's ownership and the first sale of all existing property will be taxfree. This system however may be adopted as a first stage to gain experience for the full scale introduction of capital gains tax at a later date.

RATE OF TAX: ABATEMENT FOR LAPSE OF TIME

83. It is usual to distinguish for tax purposes between short-term and long-term gains. Where both acquisition and disposal of an asset take place within a few months, the transaction is much closer to a trading operation than where there is, say, a 20-year time gap between the purchase and sale. A common provision in gains tax legislation is therefore to deem short-term gains (e.g.

18) This method was adopted in capital gains legislation in the U.S.A. and the Philippines in 1913 and in the U.K. in 1965.

purchase and sale within six months) to be income for income-tax purposes.

84. Long-term gains are usually taxed at a fixed rate appreciably lower than the rate of income tax (for example, in the U.S.A. the capital gains tax rate is half the income tax rate and subject to a maximum of 25%). Some countries however operate a scale of rates which diminishes with the length of time the asset has been held[19])

85. A tax abatement increasing with the length of time an asset has been held is in keeping with the fact that the longer an asset is owned the less the sale of it resembles a trading transaction. A rates scale of this kind is also reasonable in a country where there has been unusually heavy currency depreciation. In general, however, provided the actual rate of tax on long-term gains is moderate, it is preferable to maintain a flat rate of tax so as

(i) not to erode the tax yield;

(ii) not to give an incentive to the retention of property which is ripe for development by the owner so as to obtain a lower rate of tax on his eventual capital profit.

ALLOWANCE FOR CAPITAL LOSSES

86. Although the case for capital gains taxation includes the argument that if income is taxed there is little equity in exempting gains it is not practicable to afford equality of treatment in all respects. The case for different rates of tax has already been discussed (paragraphs 83-85) and the case for different treatment of losses is now considered.

87. Although some countries allow trading losses to be carried back against profits of previous years for tax relief purposes, in general this is a principle not ordinarily applied in the administration of taxes. Budgeting becomes difficult if the amount of tax due and collected in the financial year may be eroded by subsequent events such as the incurring of losses because of a downturn in trade. In the case of capital losses some countries allow a limited offset against income but no case is known of a country allowing such losses against the gains of prior years (except e.g. in a limited technical sense where the sale of an asset may take place before its purchase in a "bear" transaction).

88. The inequity referred to in paragraph 42 whereby a once-in-a-lifetime gain is realised and taxed and the recipient thereafter makes only (unrelieved) capital losses, is a real one but it is usually regarded as too hazardous to revenue to attempt to remove the anomaly.

89. Complete freedom to set capital losses against income even in the current year would enable the more sophisticated taxpayers to reduce their income tax liabilities by judiciously selling stocks, shares and other assets currently valued at less than acquisition cost while retaining those assets which had appreciated. At a time of economic depression the danger to revenue receipts is clearly demonstrated by experience in the U.S.A. both in the depression of the 1930's and during the Second World War. For example in 1931 taxation of capital gains in the U.S.A. produced minus $89 million (reducing the personal income tax yield by this sum) representing 36% of the total tax on individuals, while in 1941 the corresponding figure was minus $86 million although this represented only 2% of a much higher

19) e.g. Sweden reduces the tax rate successively until it becomes NIL on capital gains realised after 10 years. Ghana has recently established a 21-year time scale with rates ranging from 75% down to 10%. Israel employs a similar time-scale whereby potential liability disappears after the asset has been held for 18 years.

personal income tax yield ($3,908 million).[20]) It is not merely the quantum of revenue which may be at stake it is also the impossibility of making a useful budget estimate which takes fully equitable loss provisions out of the realm of practicability.

90. Accordingly the usual practice on capital losses is to make an allowance for these only against future capital gains and to make no allowance against income even where there is an option for the taxpayer to treat capital gains as income subject to income tax.

91. The necessary segregation of capital losses from income and its somewhat inequitable results is a further argument for providing an annual exemption limit for capital gains as argued in paragraphs 45-48.

CAPITAL GAINS TAXATION AT SOURCE

92. Although the principle of taxation at source is widespread in income tax administration it is not so easily applied to capital gains taxation. The short-lived Israeli capital gains tax on stocks and shares contained provisions for taxation at source but the decline in business (and values) on the stock exchange was so serious that the tax was abandoned after a few months.

93. In general attempts to collect tax at source by using stockbrokers as collecting agents are likely to be unrealistic because of the complexities which arise where deals by particular taxpayers are frequent and may involve many deals in the same stock. Stamp duty is often collected through the agency of stockbrokers but being usually an ad valorem tax on the gross sale value collection is mere routine.

94. It can be assumed that because of the rapidity with which transactions may sometimes be made and the fact that a taxpayer's liability or otherwise depends on the sum of his capital transactions throughout the fiscal year, it will be impossible to collect a seller's true capital gains tax at source.

ARBITRARY DEDUCTIONS

95. It then remains to consider whether it would be desirable to deduct provisional tax arbitrarily at the source. The advantage of arbitrary general deductions is that there would be little danger of tax evasion but it should be quickly pointed out that the administrative problem of repaying the tax to those who have no net gain position and in giving suitable credits to those who are taxable would be so immense as to make the system unworkable. In a depression year it might even be that virtually the whole of the tax deductions would have to be repaid. Moreover the effect of anything other than a purely nominal tax deduction would be certain to drive share transactions away from the stock exchange into private deals or even into foreign territories with serious effects on the local market and on local investment.

96. In general therefore it is wisest not to attempt deduction schemes for share transactions but, as far as anti-evasion work is concerned, to arrange for the use of information regarding share deals to be gathered at the source rather than the tax itself.

LAND AND OTHER PROPERTY

97. The prospects of deduction at source in the case of deals in real estate are somewhat more promising than in the case of stocks and shares although even in this category the initial administrative strain may be such that the processing of deductions may be an impossible burden. Little use of deduction schemes seems to have been made so far and brief details are therefore given in paragraphs 98-99 of the scheme employed in Argentina which appears to have good potential as

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20) Source: U.S. Treasury Department.

workable means of collecting at source the appropriate tax in the general run of cases. The method has particular relevance in the case of countries where there has been a not-yet-corrected tendency to currency depreciation. In these cases early collection of taxes is important both for budgetary purposes and to assist in maintaining the stability of the currency.

WITH-HOLDING OF TAX AT SOURCE: ARGENTINA

98. Argentina does not apply capital gains tax to stock and share transactions but does include property deals and other items, such as lottery wins, within the scope of its capital gains tax. In the case of lottery wins, the tax due (20%) is simply deducted at the source by the lottery authorities: gains on sale of property are taxed through the medium of the notary public, estate agent or other person professionally concerned in the deal.

99. The taxpayer selling the property must file a return giving details of the transaction The professional intermediary then transmits this document to the Tax Department for checking before with-holding the tax due—the rate of tax on the gain was 5% up to 31st December, 1964 and was then increased to 10%.

100. The taxpayer is entitled to a basic exemption of M$N 100,000 (with effect from 1st January, 1965, previously M$N 50,000) in the case of property and claims this (or what remains of it after previous transactions) as a deduction when filing the return regarding the current transaction. If his gain falls short of the exemption still due, no tax arises. The Tax Department keeps a record of the exemption due and utilised and this is one reason for referring the papers to the Tax Department to check the taxpayer's "self-assessment".

ECONOMIC EFFECTS OF CAPITAL GAINS TAXATION

101. The main immediate economic effect of the introduction of capital gains taxation is that selling of land and shares slows down owing to reluctance on the part of the holders to incur tax on their realisation profits. That effect operating by itself would cause a rise in prices.

:higher short-term tax rate

102. Where short-term gains are taxed at a higher rate than long-term gains there will be a tendency to wait the necessary period (e.g. six months) before realisation. For example, Britain's recent experience with her short-term gains tax indicated a clear tendency of taxpayers to hold shares, particularly those acquired in new issues, until six months had elapsed in order to avoid altogether the tax on realisation. The effect was to raise and maintain the price of new issues to unusually high levels for a period of six months or more.

103. The effect in Britain on property—which under the short term gains tax had to be held for three years to avoid gains tax—was that there was a growth in the availability of accommodation for rent. This applied particularly to new property in respect of which owners often found it was worthwhile to let on a lease for three years with the object of selling at the end of that time.

104. The tendency of sellers to hold off is, however, not the only effect of introducing capital gains tax. Buyers who would previously have invested in the hope of realising capital gains but for whom the prospect of taxed capital gains is less inviting than the hitherto untaxed gains will also hold off and the net result may even be a small decrease in market values generally.

:impact of capital gains tax in general.

105. The reluctance to trade may lead to a certain stagnation in stock market and property market circles which is likely to be less marked if capital gains tax is, as suggested earlier, introduced slowly in a series of stages.

106. Two points are worthy of specific mention—

(i) before and after it actually comes into existence capital gains taxation is almost certain to be the subject of animated public discussion and there will always be agitation for either raising or decreasing the effective rates. It is not usually good tax policy to start with high tax rates and reduce them later because the hope or expectation of a future reduction will inhibit transactions more than the actual existence of the tax. This is a case where the initial rate should be low enough (even 10% may be adequate to begin with[21]) so that there can be no reasonable expectation of a future reduction of rate or abolition of the tax but rather that if anything the rates are likely to be increased in the future. It is then unlikely there will be much freezing up of markets for tax reasons[22]).

(ii) the "locked in" position of holders of assets the value of which has increased considerably above acquisition cost is of course worsened by decreases in the value of money which throw up gains in money terms which do not exist in real terms. After a prolonged period of gradual currency depreciation it may in fact be necessary to provide some special relief in order to "unfreeze" the market[23]). As noted above, capital gains tax operates better where the currency is reasonably stable and it is not easy to make the tax equitable in a climate of violent currency fluctuations.

CAPITAL GAINS TAX IN VARIOUS COUNTRIES

107. Capital gains taxation of one form or another exists in over 30 countries. The table in the appendix sets out some brief comparative particulars of the tax—in all cases the data are based on the latest available information.

108. In several instances the tax is of recent origin—for example, the tax has been introduced for the first time or revised; within the last 7 years in the following countries: Argentina, British Guiana, Ceylon, Chile, Denmark, France, Ghana, Greece, India, Israel, Jamaica, Mexico, Pakistan, Portugal, and the United Kingdom. There are some notable absentees from the list of countries which employ capital gains taxation e.g. Canada and Australia.

109. The taxes employed fall broadly into two categories:—

(i) the short-term or limited-term gains tax which taxes gains, broadly speaking, only when the acquisition and disposal of the asset take place within a certain period of time; and

21) In Argentina certain capital gains were taxed at 5% during the period 1.1.61 to 31.12.64. From 1.1.65 such gains were taxed at 10%.

22) The recent British proposals for Development Charges on betterment which envisage a commencing rate of 40% with subsequent increases to 45% and then to 50% follow this principle and this feature of the proposals has received the approval of the experts.

23) This has been done on several occasions in the U.S.A. for example.

(ii) long-term gains taxes which levy tax regardless of the length of time between acquisition and disposal.

110. Countries employing the short-term gains tax include Denmark and Spain (both on securities only), Norway, Sweden, Taiwan and (up to 6 April, 1965) the United Kingdom. The "chargeable" period varies considerably e.g. in Sweden, there is exemption if an asset is held for 10 years or more—in the United Kingdom, the period was 6 months for shares and 3 years for other property. In Ghana, the tax is reduced from 75% to 10% but (exemption is not granted) where an asset is held 21 years or more.

111. As mentioned at the beginning of this treatise capital gains tax does not in general produce much revenue. There is still a good deal of controversy on some of the main features of the tax although it is generally agreed that there is equity in general principle in this form of taxation.

ESSENTIAL ELEMENTS OF A VIABLE SYSTEM OF CAPITAL GAINS TAX

112. The following features are to be found fairly generally in capital gains tax systems and would be desirable, if not essential, provisions in initial legislation to introduce capital gains tax in a developing country.

(i) Capital gains are charged at a lower rate of tax than ordinary income.

(ii) The initial rate of tax should be low enough such that any public expectations regarding future rate charges should be of increases rather than decreases. There is then no incentive to hold back land which is required for development.

(iii) short-term gains are charged at higher rates than long-term gains, the former being more nearly kin to trading income.

(iv) On disponsal of assets acquired before the introduction of the tax the taxpayer is permitted to deduct either original cost price, or the value of the asset at a subsequent date e.g. the date of introduction of the tax.

(v) An exemption is granted for capital gains below a certain figure which may be substantial in order to limit administrative work. The exemption applies in particular where the gains tax is separate from the income tax.

(vi) The scope of the tax generally excludes private chattels including motor cars but extends to other assets whether
  (a) bought,
  (b) inherited, or
  (c) received as a gift.

In the case of (b) and (c) the "cost price" to the recipient may be the market value at the date of the bequest or gift.

(vii) Exemption or abatement may be allowed in respect of capital gains made on sale of the taxpayer's residence.

(viii) Exemption may be given for gains on sale of business premises e.g. where this is part of an expansion scheme into larger premises.

(ix) The initial tax is restricted to land and property and excludes e.g. stocks and shares.

As a final recommendation it may be repeated that wherever possible a gradual approach through stamp, transfer, or betterment taxes is preferable to a direct plunge into formal capital gains taxation.

PHIDIAS C. KYPRIS:

INCOME TAX CHAOS IN CYPRUS

ACT II

This article is a continuation of my previous one published in the Bulletin in October, 1965, page 415, to which readers are referred if they want to understand fully what follows. I propose here to examine three cases, decided by the Supreme Constitutional Court of Cyprus, in order to show the labyrinth into which both the Commissioner of Income Tax and the tax-payers were led by the improvident provisions of the Constitution. Before proceeding, however, to the examination of those cases I might as well repeat at the outset the main points of those articles of the Constitution which are necessary in understanding the decisions of the Court.

Article 188: "... all laws in force on the date of the coming into operation of this Constitution shall ... continue in force on or after that date ... provided that ... any law imposing duties or taxes may continue to be in force until the 31st day of December, 1960".

Article 78, paragraph 2: "Any modification ... of any law imposing duties or taxes shall require a separate simple majority of the Representatives elected by the Greek and the Turkish Communities respectively taking part in the vote".

Case No. 1. Vasos Constantinou Kyriakides v. The Republic of Cyprus, through 1) The Minister of Finance, 2) The Commissioner of Income Tax.

The Commissioner sent to the applicant on August 10, 1961, income tax returns for completion in respect of the six years 1955 to 1960. The applicant filled the returns and returned them to the Commissioner showing his alleged income for those years. The Commissioner did not accept the accuracy of the applicant's returns and proceeded to assess the applicant's income for the years 1955-1960 to the best of his judgement. On August 28, 1961, the Commissioner served the applicant with the requisite notices of assessment. The applicant objected against the assessments as being excessive and was called at the Income Tax Office, Famagusta, for an examination of his case. No agreement was reached between the parties and the Commissioner proceeded to determine the applicant's objections reducing, in the end, the original assessments and communicating them to him on October 3, 1961.

In his application to the Supreme Constitutional Court the applicant contented that the said assessments were unconstitutional, illegal, in excess of powers and of no legal effect whatsoever.

It must be reminded here that at the time the assessments were made there was no income tax law in force. Cap. 323, the law which governed income tax in the former Colony of Cyprus, expired, by virtue of article 188 of the Constitution, on December 31, 1960, but its force was extended up to March 31, 1961. The next step in the way of income tax legislation was taken on December 29, 1961, when the three laws imposing separately income tax on Greeks, Turks and foreigners were published in the Official Gazette. So, from the 1st of April to the 29th December, 1961, there was no income tax law in existence.

The decision of the Court may be stated briefly as follows:

(a) The Income Tax Law, Cap. 323, containing, in a primary way, provisions imposing taxation which, if enacted now, would require a separate simple majority under Art. 78 of the Constitution, was not in force at the time the assessments in the instant Case were made.
(b) As at the material time there was no legislation in force the assessments were declared null and void.

The assessments were declared "null and void" and so the Revenue could not proceed to collect the tax. Of course this was not the only case pending before the Court. And the important thing is that this decision was pronounced on February 8, 1963, nearly two whole years after the expiration of Cap. 323. Professor Dr. Forsthoff, President of the Court, expressed the tragedy in simple words when he said:

"At this stage what is in issue, in the circumstances of this Case, is the interpretation and application of paragraph 2 of Article 188.

The said paragraph 2, like any other provision of the Constitution must be interpreted in a manner consistent with the meaning of its context and also, in so far as this is possible within such context, consistent with its intended object and consequences.

It is first to be observed that as a result of the operation of such paragraph 2 and the subsequent non-enactment of new income-tax legislation, the applicant, as well as a great number of other citizens of the Republic who, in the ordinary course of events, would have been liable to contribute to the public burdens, in varying amounts, by way of income-tax in respect of the period prior to the alleged expiration of Cap. 323, have found themselves in a position to allege, irrespective of the righteousness of such allegation which is not the concern of this Court, that the application of the provisions of paragraph 2 and 3 of Article 24, an Article dealing with their fundamental rights and liberties, entitles them to avoid making such contributions as above. The fact, however, remains that a considerable number of other citizens have already made such contributions and, whatever the outcome of this Case, they do not appear to have any right in law to claim a refund thereof".

Case No. 2. In Re Haji Kyriakos and Sons Ltd. of Famagusta

At the hearing of an application by and on behalf of the Director of Inland Revenue before the District Court of Famagusta, puruant to the filing of a certificate under his hand, moving the court to issue a summons under s. 9 of the Tax Collection Law, No. 31 of 1962, and to fix a date for hearing the said application, counsel for the Debtors/Defendants raised a question of alleged unconstitutionality of certain laws which was referred to the Supreme Constitutional Court as follows:

1. "Whether having regard to Articles 24, 87, 88, 144 and 188 the Law entitled 'Greek Communal Law for the Imposition of Personal Contributions on Members of the Greek Community for the year 1961, No. 16/61 and particularly sections 4 and 5 are unconstitutional.
2. Whether having regard to Articles 24, 88, 87, 144 and 188 section 9 of the Tax Collection Law No. 31/62 in so far as it provides for the collection of the tax in the present case is unconstitutional".

The Court decided that neither of the above laws was unconstitutional, so the Revenue could proceed to collect taxes already assessed under law 16 of 1961 of the Greek Communal Chamber. The value, however, of this decision was minimized by the fact that it was pronounced as late as March 21, 1963. In the meantime nobody knew whether income tax would continue to be a permanent feature of economic and fiscal life in Cyprus.

And, moreover, another case, decided also on March 21, 1963, created some doubts in the minds of many.

Case No. 3: Stravroulla Lyssiotou v. 1) The Republic of Cyprus, through the Minister of Finance, 2) The Greek Communal Chamber.

The applicant in this case was served with notices given under Law 16/1961 of the Greek Communal Chamber and which notices purported to confirm assessments which were originally made during a time that there was no legislation in force at all (Vide case No. 1 above). The President of the Court's concluding words were as follows:

"As, however, such notice 'B' purports to confirm, under Law 16/61, assessment 'B' which was not itself made under such Law but, as above stated, was made, at the time, without the authority of any Law, the Court is of the opinion that it was not possible under Law 16/61 validly to confirm an assessment which was not made under such Law 16/61 and which, in any case, was made originally without lawful authority. Should Respondent No. 2 intend to tax applicant in respect of the year of assessment 1961 the process of assessment under the appropriate legislation, has to commence ab initio".

MAX HUBERT BROCHIER:

LE CODE DES INVESTISSEMENTS EN ALGERIE

L'Ordonnance No 66.284 du 15 septembre 1966, parue au Journal Officiel de l'Algérie du 17 septembre 1966, porte Code des Investissements.

Elle abroge la loi No 63.277 du 27 juillet 1963 traitant du même domaine.

Ce Code a pour objet essentiel de pallier aux insuffisances de ladite Loi, en délimitant le cadre dans lequel est organisée l'intervention «du capital privé» dans les multiples branches de l'activité économique algérienne.

Il tient compte, d'autre part, de l'absolue nécessité de simplifier la procédure d'agrément.

Quels en sont les grands principes?

1. Les personnes physiques ou morales, qu' elles soient algériennes ou étrangères, peuvent entreprendre la réalisation d'investissements en Algérie, dans les secteurs de l'industrie ou du tourisme.
2. L'Etat algérien se réserve l'initiative de réaliser des projets d'investissement dans les branches qui seront reconnues «vitales» pour l'économie du pays.
3. L'Etat algérien pourra dans tous les secteurs s'associer, au sein de «sociétés d'économie mixte», à des entreprises à capital étranger ou algérien.

Quels sont les avantages et garanties qui y son fixés?

A. L'Etat algérien s'engage à partager les soucis des investisseurs pour ce qui est de l'exploitation des entreprises visées par ledit Code des Investissements.
B. Les entreprises qui seront agréées à ce titre, ne pourront faire l'objet d'une «décision de reprise» par l'Etat algérien, que lorsque les exigences du développement économique de l'Algérie la rendront impérative.
C. Dans ce dernier cas, la reprise donnera plein droit à une indemnité, nettement définie dans l'Arrêté d'Agrément quant à son montant et aux délais de remboursement et de transfert.
D. Cet arrêté d'agrément précisera les conditions de transfert des bénéfices qui seront réalisés par lesdites entreprises.
E. Les avantages accordés relèvent du domaine de la fiscalité: le bénéfice d'un régime fiscal stabilisé sera accordé dans le cas où les entreprises passent des marchés à long terme, et ont, de ce fait, besoin de connaître leur prix de revient définitif, ainsi que la rentabilité des opérations envisagées sur une longue période.
F. Les garanties et avantages ont surtout pour but de mobiliser des ressources «internes» et des «capitaux étrangers» en vue de la réalisation d'investissements qui seront utiles au développement de l'Algérie, en vue de susciter l'achat par les entreprises installées dans ce pays, du matériel fabriqué dans le pays.

Les principes de cette ordonnance sont les suivants:

L'initiative de la réalisation de projets d'investissement dans les secteurs «vitaux» de l'économie algérienne revient à l'Etat.

Cependant l'Etat peut faire appel au capital «privé» pour la réalisation de ces projets.

Les sociétés d'économie mixte (association de l'Etat, et du capital privé étranger ou algérien) doivent voir leurs statuts approuvés par décret. Ils comporteront notamment:

- La faculté pour l'Etat de racheter tout ou partie des actions dont il n'est pas propriétaire;
- les conditions dans lesquelles il pourra exercer cette faculté;

– la faculté pour lui d'exercer un droit de préemption ou d'agrément en cas de vente, transfert ou cession d'actions dont il n'est pas propriétaire.

Au cas où l'intérêt public exigera la reprise, par l'Etat algérien, d'entreprises bénéficiant des disposition dudit Code, une telle mesure ne pourra être prononcée que par un texte à caractère «législatif»: elle emporterait, de plein droit, paiement dans un délai maximum de 9 mois d'une «indemnité», égale à la valeur nette, fixée contradictoirement à dire d'experts, des éléments du patrimoine social repris par l'Etat.

Ladite indemnité sera majorée:

– du montant non amorti des frais d'établissement ou autres valeurs incorporelles correspondant à des dépenses effectives qui n'ont pas été prises en considération pour le calcul de cette indemnité;

– d'intérets calculés au taux légal pour une durée de deux ans sur le montant de ladite indemnité.

Cette indemnité étant transférable à l'étranger, si le bénéficiaire est lui même étranger, et si l'investissement a été réalisé à l'aide de fonds importés en Algérie.

Pour ce qui est du recrutement du «personnel», les entreprises ont le droit de recruter le personnel étranger «spécialisé», qui leur est nécessaire. Leur limite reste fixée dans la décision d'agrément. La liberté de fixation de résidence et de déplacement lui est garantie.

Pour ce qui est des «droits à transfert», en voici les dispositions légales:

– Transfert de la partie distribuée des «bénéfices annuels nets» de l'entreprise, établi après déduction des amortissements ou provisions nécessaires et compte tenu de l'importance de son endettement.

– la partie distribuée des bénéfices n'étant cependant transférable que dans la proportion qui peut exister entre les participations étrangères dans les fonds propres de l'entreprise, et le total de ces fonds propres, et sous la condition que ces participations correspondent à des importations effectives de capitaux en Algérie.

– Les transferts de «bénéfices à l'étranger» ne pouvant dépasser annuellement 15 pour-cent du montant des participations étrangères, dans les fonds propres de l'entreprise en Algérie.

– Les bénéfices transférables réinvestis étant considérés comme une importation de capitaux.

Transfert, après encaissement, du produit de la cession ou de la liquidation de l'entreprise, ou de la cession des actions, pour autant que l'acquéreur soit une personne physique «algérienne» ou une personne morale »sous contrôle algérien», ou que, dans les autres cas, la Banque Centrale de l'Algérie ait autorisé l'opération.

Les entreprises agréées peuvent bénéficier des avantages fiscaux ci-après:

– Exemption totale ou partielle du droit de mutation à titre onéreux, dans la mesure où il s'agit d'acquisitions immobilières, destinées exclusivement à l'activité agréée.

– Exemption totale, partielle ou dégressive de l'impôt-foncier, pendant une période qui ne peut excéder 10 ans.

– Octroi du taux réduit de la taxe unique globale à la production pour les acquisitions de biens d'équipement, ou ristourne de la taxe afférente aux biens d'équipement fabriqués en Algérie.

– Octroi de délais, échelonnés au maximum sur la durée de l'amortissement industriel, pour le paiement des droits de douane et de la taxe unique globale à la production se rapportant aux biens d'équipement nécessaires à la réalisation du projet.

– Exonération totale, partielle ou dégressive de l'impôt sur les B.I.C. pendant une période ne pouvant excéder une durée de 5 ans et pour un montant annuel de bénéfices ne pou-

vant dépasser 20 pour-cent des fonds propres investis dans l'activité agréée; ces avantages fiscaux ci-dessus énoncés ne pouvant être consentis que dans la mesure où les conditions initiales d'exploitation de l'entreprise, ne lui permettent pas de supporter immédiatement des charges fiscales normales. A cet égard il sera tenu compte des éléments suivants:

A. du rapport existant entre le montant des investissements et le nombre d'emplois permanents créés;
B. des effets indirects de l'investissement sur les activités connexes;
C. du rythme de la formation professionnelle et la promotion des cadres nationaux;
D. du secteur économique et de la zone géographique d'implantation;
E. du volume de la production destinée à l'exportation, ou se substituant à des importations;
F. du volume du capital nouveau importé.

Dans des cas spéciaux, les entreprises peuvent bénéficier d'avantages spéciaux, tels qu'une garantie subsidiaire donnée par la caisse algérienne de développement pour le compte de l'Algérie, afin de faciliter l'obtention d'avances bancaires à court terme sur warrant industriel pour le financement de fabrications ou de stockages; – et également elles peuvent bénéficier d'une garantie que le taux de certains financements à moyen ou long terme ne dépassera pas le chiffre maximum fixé lors de l'octroi de l'agrément; enfin elles peuvent bénéficier de la garantie de l'Etat algérien pour leurs emprunts d'équipement.

Telles sont les garanties, tels sont les avantages fiscaux et financiers du Code des Investissements en Algérie, accordés aux entreprises à capital étranger ou algérien, agréées. Les dispositions de ce Code contiennent 33 articles lesquels délimitent notamment le cadre dans lequel est organisé l'intervention du «capital privé» dans les diverses branches de l'activité économique algérienne.

Le titre II (articles 20 à 27) traite essentiellement de l'Agrément. Disons à ce sujet simplement que pour les «investissements étrangers», les critères ci-après sont pris en considération:

– Ouverture de marchés extérieurs d'exportation;
– importance de la valeur ajoutée dégagée en Algérie par l'entreprise;
– degré d'utilisation des matières premières locales;
– niveau de couverture par des fonds propres, de l'investissement à réaliser.

Les demandes d'agrément doivent être adressées:

– au Préfet du département si le montant total de l'investissement ne dépasse pas 500.000 D.A. et qu'aucun avantage financier n'est sollicité;
– au Secrétariat de la Commission Nationale des Investissements dans les autres cas.

* * * * DOCUMENTS * * * *

PROPOSED SALES TAX REFORM IN CANADA

On February 24, 1967, the Royal Commission on Taxation (Carter Commission) submitted its long-awaited Report on the Canadian tax structure. The lengthy and complex six volume work, now in the Bureau's library, contains literally hundreds of conclusions and recommendations which, if implemented, would make fundamental changes in Canadian taxation concepts, principles and practices.

A summary of the Commission's main findings will be published in the next issue of the Bulletin. In this issue, we direct attention to the general structure and motives behind the proposed sales tax reform, but one of the recommendations, which we think to be of special importance to all concerned with the concept or neutrality of sales taxation.

EDITOR'S NOTE

The 11 per cent federal sales tax now applied at the manufacturing level to most consumer goods should be abolished and replaced by a 7 per cent federal sales tax to be applied at the retail level to both consumer goods and services, the Royal Commission on Taxation recommended February 24, 1967.

Food, shelter and producer goods would be exempt from the proposed retail tax. In fact most of the present exemptions from the manufacturer's tax would continue to apply and some additional items—prescription drugs, for example—would also become exempt under the Commission's proposals.

The Report recommends that initially only a limited number of defined services should be taxed, in order to ensure that only those services not entering directly into production are subject to tax. But the Commission suggested that eventually a broad range of consumer services should be taxed.

The 7 per cent rate at the retail level would raise almost as much federal revenue as the 11 per cent rate at the manufacturer's level—which many consumers are seldom conscious of paying—but the average federal sales tax burden on those with incomes below $10,000 a year would decline by about 10 per cent.

Because the proposed 7 per cent rate would mean some reduction in federal sales tax revenues, the change in the level at which the sales tax is applied should not cause any general price increases, the Commission said. Where a province has a general provincial sales tax rate of 5 per cent, the Commission's proposals would result in a total tax at the retail level of about 12 per cent. Nine of the provinces—all except Alberta—now have either enacted or announced sales taxes ranging from 4 to 6 per cent.

If the federal government accepts the new retail sales tax base and rate, the Commission said it then should negotiate to have the same tax base adopted by the provinces, which then might do the entire job of collecting sales taxes.

The provinces should be permitted to impose an indirect retail sales tax, the Commission

recommends. At the present time the constitution limits the provinces to direct taxes.

The Commission indicated it would prefer to see no federal sales tax at all in Canada. But it could not countenance the massive increase in income taxes that would be necessary to match the revenue that a federal sales tax yields.

In designing the proposed new federal retail sales tax, the Commission provided specific exemptions to prevent "regression"—the unfair burden of tax imposed on low income families due to the fact that they spend a heavier proportion of their incomes on taxable goods and services than upper income families.

Exempt from the proposed new tax would be all food, including soft drinks, candy and inexpensive restaurant meals; shelter, including houses and rents, and fuel and electricity; all educational services; the services of hospitals, doctors, dentists, nurses, lawyers and undertakers; books, newspapers and magazines; and prescription drugs, and appliances and devices for the handicapped. Also exempted would be producer goods, goods for export, and finished buildings and structures. Producer goods would include raw materials and unfinished goods, production equipment and machinery, and capital goods used in distribution and services. The government recently enacted legislation providing for the removal of the tax on production equipment in stages; the Commission recommends it be removed immediately.

Eventual removal of sales tax on building materials also was recommended in today's Report. But the Commission said that, while it could find no economic or social justification for imposing such a tax in the first place, it now is impossible to lift it immediately because the federal revenue loss would be too great. Meanwhile, shifting the tax to the retail level and applying a lower rate would result in an effective 30 per cent cut in the tax on most building materials.

The Commission recommended that special excise taxes on certain so-called «luxury goods» be repealed immediately. This would remove existing levies from radio and TV sets, phonographs, electronic tubes, cosmetics and toilet goods, clocks and watches, jewellery, playing cards, coin-operated amusement machines, cigarette lighters, matches, pipes, cigarette holders and cigarette-rolling machines.

But the excise taxes and excise duties on alcohol and tobacco products should be retained, the Commission said. These "extraordinarily heavy" levies now yield an enormous amount of revenue—about 10 per cent of all federal budgetary revenues—and have widespread public acceptance, "facilitated by the prevailing attitude that these goods are injurious and should be expensive."

All told, the federal retail sales tax as proposed by the Commission would apply to a wide range of goods which in 1964 had a retail sales value of about $17 billion, including about $4 billion worth of building materials. The taxable sales would include—on the basis of 1964 personal expenditures—about $4 billion in automotive products, $2.8 billion in clothing and footwear (there would be no special exemption for children's clothing), $1.2 billion in furniture and appliances, and about $1 billion worth of alcoholic beverages.

Services that are proposed to be taxed immediately—those that generally do not enter into production costs—had a sales value of $4 billion as of 1964. About one quarter of this was telephone and telegraph services. Another quarter was accounted for by hotel, motel and similar accommodation and services (excluding liquor). The balance would include auto and other kinds of repairs and services by retail establishments, laundry and

dry cleaning services, restaurant meals above some tax-exempt minimum, barber and beauty shops, dressmaking and photographic services, etc.

All told, the Commission estimates that total federal sales tax revenues as of 1964 would have been $1,472,000,000. This is $125,000,000 less than was yielded in that year by the 11 per cent manufacturer's sales tax and the particular excise taxes that the Commission proposed should be removed.

The Commission proposes this change in the level at which sales tax is levied as a means of achieving a measure of neutrality in the impact of the sales tax. The application of the tax at the retail level would ensure that all taxable goods bore a similar element of tax, and that many of the present problems of determining the amount that should be taxed would no longer exist. The exemption for producer goods and exports would be more readily administered. Imports would clearly bear the same tax as domestically produced goods.

The retail tax automatically and simply achieves the neutrality that a tax levied at earlier levels in the process of production and distribution cannot achieve. Regardless of the distributional channels used, of who advertises, packages or imports, etc., the cost elements that ultimately determine the selling price of an article to the consumer converge at the point of imposition of a retail tax.

The Commission said that only at this tax level can it be said that neutrality is achieved without sacrificing simplicity, or that simplicity is achieved without sacrificing neutrality.

The Report states that a retail tax avoids the alleged pyramiding effect—that is, the marking-up of the tax element in the price of goods as they pass through the various stages of distribution. In addition, only a tax at the retail level can avoid the inequities that inevitably arise with a tax at any other level because some entrepreneurs must hold tax-paid inventory.

The Commission also recommended that the federal government should try to negotiate an exchange of more sales tax room for the provinces in return for more direct (income) tax room for the federal government. The Report opposed any further abatement of personal and corporation income taxes to the provinces.

Meanwhile, sales tax exemptions for purchases by other governments and their agencies should be eliminated, the Commission said. If necessary, they could be compensated through increased grants or other fiscal arrangements. This would not change their net position, but would eliminate costly administrative problems and the discrimination that would arise when government agencies use tax-exempt goods and services in competition with non-exempt businesses.

One large administrative problem would arise in shifting the federal sales tax to the retail level: goods on which the manufacturer's tax already was paid would be included in inventories at change-over time. To avoid double taxation—the piling of the new retail tax on top of the manufacturer's sales tax which already had been paid—the government would have to postpone about $175,000,000 in revenue from the new tax, the equivalent of one and one-half months of federal sales tax revenues. The Commission considers this a justifiable price to pay for the various benefits in the new tax.

What would the tax transition do to retail prices?

"The full blaze of national publicity that would accompany the change of the sales tax base should exert a restraining influence on those manufacturers who have the market

power to raise prices and who would be tempted to capitalize on the transition", the Commission said.

"However, the combination of necessary price increase on certain goods, and the uncertainty of retailers as to the precise amount of tax that had been concealed in their purchase prices under the manufacturer's tax, could encourage some manufacturers and merchants to increase their prices.

"It is also possible that the prices of certain types of goods, notably goods that have traditionally carried a specific retail price, and those that are commonly subject to "suggested retail prices", might be rigid enough to continue beyond the transitional interval, thereby imposing higher costs on consumers.

"It seems reasonable to expect, however, that competition would force the appropriate price adjustments within a relatively short period of time. Nevertheless, we feel that a concerted public information programme, to inform individuals and firms as to the substance and mechanics of the change of base, would be necessary to increase the competitive pressures."

Variation in spending patterns among households would result in some variations in the amounts of sales tax paid on goods and services purchased by families with a given income. But such variations are small, compared with variations in income taxes. The following table shows the estimated change in average federal sales taxes paid by families in different income classes under the current and proposed systems:

Income Class	Average Federal Sales Taxes paid		Average Change in Tax	Percentage Change
	Current	Proposed		
Less than $2,000	80	78	−2	−3
$2,000– $2,999	144	131	−13	−9
$3,000– $3,999	212	187	−25	−12
$4,000– $4,999	252	218	−34	−13
$5,000– $6,999	347	303	−44	−13
$7,000– $9,999	503	435	−68	−14
$10,000 and over	722	856	134	+18
All classes	269	248	−21	−8

(Press Release)

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OPTIMALISATION DES DEPENSES GOUVERNEMENTALES

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Travaux de la XXIIème session de l'Institut International de Finances Publiques à York, 13-17 septembre 1966

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First Independence Budget of Guyana

Paul Bultynck †

C'est avec une profonde tristesse que le Bureau International de Documentation Fiscale fait part du décès survenu subitement le 11 avril dernier à l'âge de 49 ans de Monsieur Paul Bultynck.

Il était membre du Conseil de Patronage du Bureau et nous perdons en lui un ami à qui il n'était jamais fait appel en vain. A tout moment il se tenait à notre disposition pour nous prodiguer ses conseils éclairés et nous faire profiter de sa riche expérience.

Le Bureau présente à sa famille ses condoléances les plus sincères dans la perte cruelle qu'elle vient d'éprouver et que le Bureau partage avec elle.

* * * * ARTICLES * * * *

BOMCHIL PINHEIRO CLARO LAVALLE & BADO:

ARGENTINA MODIFIES BASICAL ASPECTS ON TAX AND EXCHANGE MATTERS*)

EXCHANGE RATE MODIFICATION AND ADDITIONAL MEASURES

Recently the Minister of Economy and Labor of Argentina, Dr. Adalberto Krieger Vasena announced officially that the pattern of Exchange of the Argentine peso in relation, with the dollar which was lately of 255 for a dollar, remains fixed at 350 pesos. These measures were completed with the necessary written resolutions of the Central Bank. The commented new Exchange rate consists concretely in the fact that the Central Bank acquires foreign currencies at this rate. So we can say that 350 pesos is the pattern of Exchange existing in the "Exchange Free Market". What has been said does not stop another existing market called "parallel" in which the relation of Exchange dollar-peso was even more unfavourable for the latter.

The Government announced that this devaluation of the peso was one of the measures that are taken to definitively repress inflation. The Minister of Economy reminded in his public speech that a similar measure of "anticipated devaluation" was taken by Mexico in 1954 and by Spain and France in 1958.

As the significative devaluation of the peso can produce very important benefits in favor of exporters, these will have to pay a new tax which will vary according to the products and will oscillate between 16 and 25%. This new tax eliminates the retentions system. At the same time inflation customs duties will be basically reduced in order to collaborate to stop the increasing cost of living.

Another measure taken, consists in modifying in general the customs duties avoiding the benefit of excessive customs protection to the industries considered as "non-economical". This devaluation of 43% of the peso (from 245 pesos to 350) is obviously a measure which highly favours exporters. Additionaly it might satisfy the requirements of the International Monetary Fund which most probably considers this measure as a necessary one to give stability to the Argentine Economy.

Moreover, important loans were announced which will be granted, in a very near future, by international organizations to finance development projects in Argentina.

*) This article is a follow-up to the article "Corporations and Taxation in Argentina", published in the March 1967 issue of the Bulletin and prepared under the direction of "Le Cabinet Juridique spécialisé en Droit Sud Américain à Paris, Bomchil Pinheiro Claro Lavalle & Bado".

MODIFICATION OF TAX REGULATIONS

March 6th a tax reform law modified several existing laws related to income tax, sales tax, excise taxes on alcohol and others, and stamp tax.

This new regulation established also two new taxes: a real estate tax, and another one on loans.

Regarding the modifications of income tax, we can point out that it will mean for the standard tax-payer an important annual reduction.

In the message sent by the Minister of Economy of Argentina to the President it stood out clearly that the tax reform is part of a plan of measures tending to give the public sector a larger productivity and efficiency and to destroy wholly and simultaneously all the causes which brought inflation.

The same message insists on the substantial reduction on income tax for all physical tax-payers. Deductions authorized by the law to reach from the rough income the taxable net income have been increased.

The standard tax payer (married with two children) with a monthly rough income of 100.000 pesos arising from his personal work performed as an employee, in the former system which has been modified, was paying 6,62% or 85.000 pesos and now will pay 1,29% or 16.600 pesos only.

Doubtlessly the most important point of the income tax reform resides in this reduction of the rates for the fourth taxpayer class which is the case of the liberal professions and the case of the personal labour performed as an employee.

The following comparative synopsis shows the different tax payer situations between the former system and the new one. Differences between the two percentages paid (before and now) by the tax-payer are pointed out.

Fourth Class (Liberal professions, etc.)

Net monthly income (1) pesos	Net yearly income pesos	Annual taxes (2)				Differences (in less)	
		new legislation pesos	average rate (3)	former legislation pesos	average rate (3)	pesos	%
50.000	600.000	—	—	59.490	9,91	59.490	100
100.000	1.200.000	94.920	7,91	288.870	24,07	193.950	67,14
125.000	1.500.000	179.600	11,97	415.510	27,70	235.910	56,78
200.000	2.400.000	467.280	19,47	814.970	33,95	347.690	42,66
250.000	3.000.000	682.960	22,77	1.090.970	36,36	408.010	37,40
300.000	3.600.000	910.960	25,30	1.369.790	38,05	458.830	33,49

(1) Net monthly income for 12 months.

(2) In order to compare homogeneous situations, deductions for representations and travelling expenses that can be done with invoices in the new regime (General Resolution n° 913 of General Tax Direction) are not taken in consideration.

(3) On net yearly profit.

Fourth Class (Work performed as an employee)

Rough monthly income (1) pesos	Rough yearly income (2) pesos	Annual Taxes (2)				Differences (in less)	
		new legislation	average rate (3)	former legislation pesos	average rate	pesos	%
50.000	641.600	—	— —	—	—	—	—
100.000	1.291.600	16.650	1,29	85.484	6,62	68.834	80,52
150.000	1.941.600	160.367	8,26	311.138	16,02	150.771	48,46
200.000	2.591.600	339.540	13,10	558.915	21,56	219.375	39,25
250.000	3.241.600	523.326	16,42	820.174	25,30	287.848	35,10
300.000	3.891.600	747.489	19,20	1.086.284	27,91	338.795	31,19

(1) 8400 pesos of family salary are included.
(2) Monthly income for 13 months – one month of family salary which does not produce "aguinaldo" (New Year gratification) is deduced.
(3) On rough monthly income.

The message of the Minister announced also the project to eliminate the multiplicity of taxes within a very near future. The same added that the reform will be completed during the present year. There is a tendency to extend the basis of the tax so that individually lower taxes will be paid by everybody, according to his real tax payer capacity.

Now we are going to analyse each one of the modifications produced in relation to the income tax, eventual profits tax, stamp tax, excise tax and sales tax.

Later on we will explain briefly what is foreseen by the two new taxes which have been established real estate tax and loans' tax.

I. MODIFICATIONS INTRODUCED IN THE INCOME TAX LAW

1. Article 19, paragraph 1) established among tax exemptions the salaries paid to Congressmen. This paragraph has been abolished.

2. Another paragraph is added to this article 19 which establishes exemptions for the payment of income tax, including the amounts received by the exporters as "taxes reimbursements".

This modification was necessary to clear out any doubt of interpretation. Moreover it gave full force to the profit represented in favour of the exporters the refunding of sums established by a legal mecanism existing in Argentina in order to strengthen the increasing of "non traditional exports". Now the total sums received by exporter are considered a profit which is not taxable as we said.

3. In article 20, amounts established in favour of the physical tax payer have been modified. Those are the "not taxable income". These sums have been increased to 192.000 pesos per annum and for other taxpayers of this class to 504.000 pesos yearly.

4. Another deduction established by the income tax law in Argentina, called "deduction for family charges" foreseen in the article 21 of the law, was also increased in the following way: for the husband or wife from 24.000 pesos to 96.000 pesos, for each child from 24.000 pesos to 48.000 and for the other persons that the tax payer has at his charge, from 9.000 pesos to 18.000.

5. Article 34 of the income tax law considers the cases of expenses which cannot be proved

by documents and that the law qualifies as "no justified", in consequence, to be deduced of the concept of net taxable income. These expenses were taxable of 53%. The new law reduces the rate to a 50%.

6. In the article 62 which is in the Deduction section and refers to the sums that the tax-payer may deduct from his annual income to reach the amount on which the tax will be calculated, paragraph o) considers the medical; odontological, laboratories, X rays, medicines bills authorizing a significative amount for such items. Also a certain amount can be deducted without proofs. The modification authorizes now this last deduction not only to favor the taxpayer, but also the persons whom he has at his care.

7. In that same article 62, paragraph j) besides establishing that sums given to thirds by the tax payer can be deducted from the rough income to reach the net income which pays tax, il will permit to consider the 10% of the donations as a down payment of the same tax.

This aspect has been abolished by the tax modification which we comment and therefore it is not lawful to compute as down payment of 10% of the donations.

8. A modificatory law on the income tax which was the no 16.656 established in its article 3, point 23 the exemption of tax in favor of judges referring to their pensions. This exemption has been abolished.

9. The article 86 of the law on Income taxes establishes the percentage scale for the physical tax-payers to pay this tax. These scales have been modified, being the actual ones as follows:

Net yearly taxable profits		Will pay		
over	to	pesos	more	on the exceeding of pesos
	50.000	—	8%	—
50.000	75.000	4.000	10%	50.000
75.000	100.000	6.500	12%	75.000
100.000	125.000	9.500	14%	100.000
125.000	150.000	13.000	16%	125.000
150.000	200.000	17.000	18%	150.000
200.000	250.000	26.000	20%	200.000
250.000	300.000	36.000	22%	250.000
300.000	400.000	47.000	24%	300.000
400.000	500.000	71.000	26%	400.000
500.000	750.000	97.000	28%	500.000
750.000	1.000.000	167.000	30%	750.000
1.000.000	1.500.000	242.000	32%	1.000.000
1.500.000	2.000.000	402.000	34%	1.500.000
2.000.000	3.000.000	572.000	38%	2.000.000
3.000.000	4.000.000	952.000	42%	3.000.000
4.000.000	5.000.000	1.372.000	46%	4.000.000
5.000.000	—	1.832.000	50%	5.000.000

All the modifications to the law on Income taxes which we have commented are in force for the private tax payer referring to their income from January 1st of this year.

Referring to the traders the law will be also applied on incomes appearing on Fiscal years that will end after January 1st 1967.

II. CAPITAL GAINS TAX

This tax existing in Argentina is payable on profits obtained by physical or juridical persons, derived from sources not taxed by the Income tax law provisions.

In order to calculate the amount that will be paid, the "non taxable profit amount" was 100.000 pesos, being increased now to 200.000 pesos.

So the article 10 of that same law has been modified and since January 1st of the present year the first 200.000 profit pesos are not calculated to pay the tax rate.

III. STAMP TAX

Changes produced in this tax law will be in force from April 1st of the present year.

1. Argentine stamp tax law states a reduced rate for agreements on goods, shares, securities, etc. when the same has been registered in a stock market.

The rate in that case was 1 0/00 increased now to 2 0/00

2. Paragraphs e) and f) article 36 have been modified in such an insignificant detail that they do not deserve any further comment.

3. Article 49 of the stamp tax law had established a one peso rate of each bank check being increased now to two pesos.

4. Article 50 forset 150 pesos for each power of attorney, increased now to 500 pesos.

5. Stamp tax law forset a special taxation called "taxes on legal proceedings". This latter taxation is paid by parties involved in a law suit and calculated on the amount of the same. Rates have increased in such cases too.

IV. INTERNAL TAXES

The law on internal taxes has also been modified and enters in force from April 1st of the present year.

We call internal taxes in Argentina the taxes on tobacco, alcohol, lighters, fuels and other goods whose tax is paid by the producer and the tax rate is incorporated to the cost price. The changes are established mostly to make active the tax-collection but the percentages on alcohol lighters, beauty products have been increased, and methyl alcohol is now paying such tax while in the past only ethyl alcohol used to pay it.

1. The article 5 of the same law has suffered a small modification on detailed aspects of the way to pay this tax in the cases of auctions of the "Banco de la Municipalidad de Buenos Aires" (Buenos Aires City Hall Bank).

2. The article 39 -included in the chapter on alcohols—has been slightly changed adding methyl alcohol and increasing the rate which was of 15 centavos per liter to 20 centavos for both methyl and ethyl alcohol.

3. Articles 40, 41, 54, 56 have been modified only in details which are not worth commenting.

4. Article 43 has been modified increasing the rates on imported alcohols.

5. Article 51 has suffered also a change, it is on the necessary government authorization to be able to install new distilleries when they have a production capacity superior to 20 hectoliters per day.

6. Article 60 of the internal law which we comment does not establish the rates paid by spiritual beverages, alcoholic drinks in general, whyskies and cognacs. The new law has increased the rates in each of these cases.

7. The tax on lighters and beauty products has been increased, modifying articles 61 and 63 of Internal taxes law.

We have to notice that these rates increase is only the necessary fitness due to the loss of the adquisitive value of the Argentine peso and the increase of prices.

V. SALES TAXES

The sales tax has also been modified and enters in force from April 1st of the present year. The changes consist only in increasing this tax

on some goods, considered luxury. The highest rate of 20% is paid now by transistorized shaving machines, cameras, television sets, etc. Home articles as washing machines, aspirators and cars which paid a 10% rate have been increased to 15%.
Vegetal or animal margarine and air-craft gasoline pay the 3% rate.

NEW TAXES

As we commented at the beginning two new taxes have been created in Argentina. Tax on loans and the real estate tax.

VI. TAXES ON BANKS AND FINANCIAL ENTITIES LOANS

Entering in force from April 1967 up to March 1968, exactly for 12 months a new "extraordinary" tax has been created of a yearly 2% on balances, paid by the one who receives the loan simultaneously with the interest. The national organism called Direccion General Impositiva is in charge of the tax collection and its control. This tax will be ruled by the National Tax Proceedings law n° 11.683.

VII. REAL ESTATE TAX

Another tax called 'of emergency' meaning to be applied only once has been created. The taxpayer will make a unique payment of this tax. This tax on the real estate property, urban or rural, is of 1% on the amount established by the existing fiscal valuation. In the national, provincial or municipal organisms there are "fiscal valuations" basis on which the governmental organisms collect taxes. Generally the fiscal valuation is lower than the real commercial price of the property especially when this is not occupied or occupied by tenants whose contracts are not extended by the law of lease. When, on the contrary, the property is occupied by tenants whose contracts are extended by the law, the fiscal valuation is higher than the real commercial price.
The law which has created the tax we are commenting foresees that in the cases in which there is no fiscal valuation the tax will be paid on 70% of the sum of money spent to buy the property or invested in its building. This tax will not be deductible in the liquidation of the income tax.
We can point out that the Argentine Government authorities have established that the owners of the properties are responsible for the payment of this tax, these can recover from the tenants the amount of the tax when the property is occupied in the conditions we mentioned, with contracts extended by the laws which protect tenants in Argentina.
This last measure has been taken, without any doubt, because of the great protection granted to the tenants by the State and also because of the low income-producing of the properties occupied with contracts extended.
The law establishes also that a notary public cannot execute a contract of transfer of property without having credited that the payment of the tax has been made. National, provincial or municipal authorities are not allowed to attend any application unless the payment of the tax has been proved.
Regarding this tax an additional payment system very onerous has been created when the payment is not made in due time. For one month of delay, the additional tax is of 50% and for two months of 100%. The additional payment reaches 500% when the delay is superior to three months.
Finally, when the property is divided between a bare-owner and an usufructuary, the owner is responsible for the payment of the tax but he is entitled to recover 50% of the tax paid from the usufructuary.

* * * * DOCUMENTS * * * *

MAIN PROPOSALS CANADIAN ROYAL COMMISSION ON TAXATION

In the April 1967 issue attention has been paid to the general structure and motives behind the proposed sales tax reform, which is one of the recommendations in the Report on the Canadian tax structure of the Carter Commission. In this issue we are drawing attention to the main findings of the Report.

EDITOR'S NOTE

—A complete transformation of the Canadian tax system designed mainly to achieve equity—taxation according to the ability to pay—has been recommended by the Royal Commission on Taxation.

The proposed new system would mean tax reductions for most low income and middle income families, increased Canadian investment in Canadian enterprises without discriminating against foreign investors, and greater economic efficiency—all this without reducing federal tax revenues.

Hundreds of conclusions and recommendations are included in the massive six-volume, 2,600-page Report of the Commission, headed by Kenneth LeM. Carter of Toronto. The Report is the result of four and one half years of work by the six-member Commission, aided by a research staff that at one time numbered 150 lawyers, accountants and economists.

Following are the Commission's major proposals in brief:

—The ability-to-pay principle would be reflected in a new "comprehensive tax base" that would include, for tax purposes, all net gains in purchasing power, including capital gains and windfalls and many other forms of real income that now are tax-exempt.

—Taxation of capital gains would not be retroactive. Only those increases in the market value of assets that take place after the adoption of the proposed new system would be subject to tax if realized. There would be a $ 25,000 lifetime exemption on gains realized on the sale or disposition of owner-occupied homes and farms. Capital losses could be deducted from any income.

—Rates of personal income tax would be greatly reduced. Instead of today's easily avoided 80 per cent the top rate would be 50 per cent. However, as many persons have substantial income which now is untaxed, they would pay higher taxes despite the lower rates. But those who rely mainly on wages and salaries would pay less. A number of existing deductions would be replaced by tax credits, more valuable for low income families. All told, an estimated 46 per cent of the country's 7,000,000 taxpayers would get income tax cuts of more that 15 per cent under the new system.

—New tax-paying units would be created and a different rate schedule would apply to each—families (parents and children under 21, or under 25 if they are taking post-secondary education) and individuals. Families would be required to pay tax on their aggregate income. Transactions within the family would not be taxed; for example, there would be no tax on a man's estate when it passed to his wife or dependent children.

—The existing 11 per cent federal sales tax applied at the manufacturing level would be moved to the retail level, at a reduced rate of 7 per cent. The tax would be extended to certain services. Food, shelter and production goods, as well as exports, would continue to be exempt. Prescription drugs would also become exempt. The special excise taxes on some so-called luxury goods would be eliminated. The net result would be an average drop of about 10 per cent in federal sales tax paid by families with incomes below $ 10,000.

—There would be a major change in the way corporation income is taxed. Tax would still be *collected* from corporations, but at a single flat rate of 50 per cent; the present lower rate of 21 per cent on the first $ 35,000 of corporation income would be abolished, with its investment-incentive element replaced by rapid-depreciation privileges for new and small businesses.

—But corporate and personal income taxes would be "integrated", that is, every Canadian shareholder of a Canadian corporation would be granted a 100 per cent credit for taxes paid on his behalf by the corporation. Although this major new benefit would be partly offset by the full taxation of share gains, it would increase the flow of Canadian savings—both individual and institutional—into Canadian equities.

—While realized share gains would be taxed at full rates, for most corporations the taxable gain would only be part of the total gain in the price of their shares. Because of integration, share gains for tax purposes would include only the gains in excess of those resulting from the retention of earnings by corporations.

—Co-operatives and credit unions would be treated in such a way that they would have neither tax advantages nor disadvantages relative to other forms of business organization.

—Inefficient concessions to industry would be abolished. This would mean the end of the present three-year income tax exemption for new mines, and of depletion allowances now granted to both the mining and petroleum industries. While the smaller companies would be little affected, the taxes collected from a few large companies would increase sharply.

—Major changes in the tax treatment of various kinds of contractual saving would make Registered Retirement Income Plans more attractive. Tax collections from life insurance companies would be substantially increased as a result of taxing them like other businesses.

—Gifts other than those between members of a family unit would be included in the comprehensive base and would be taxed like other income. But there would be substantial annual and lifetime exemptions on such gifts. Gift and death taxes as such would be abolished.

—An employee's expenses in earning his income would be recognized for tax purposes, just as business expenses are. He would be able to claim actual expenses (but not those for commuting), or could claim an optional standard deduction of 3 per cent of his income up to a limit of $ 500. Special tax credits would be given to working mothers.

—Tough, arbitrary limits would be placed on travelling and entertainment costs to stop "expense account living". Any businessman who overspent these specified daily limits would be forced to take the excess into his own personal income, and pay tax on them.

—Many of these proposals, especially those changing the tax base, would have profound implications for federal-provincial fiscal relations. The Commission said Ottawa should not make any further abatements of personal income tax to the provinces, and

should take over the entire job of taxing the income of corporations. Provinces which now have sales taxes—all except Alberta—would be encouraged to adopt the proposed federal sales tax base, and collect all sales taxes. Any further "tax room" provided by the federal government to the provinces would be through reducing the federal sale tax rate.

—Federal tax collection and administration would be moved out of the Department of National Revenue and into a new, independent, non-political Board of Revenue Commissioners, which would report fully to the public on its operations. Commissions rather than government departments are used to collect taxes in both the United States and Britain. A new Tax Court would be established, replacing the existing Tax Appeal Board.

The tax system recommended by the Commission would raise about the same revenues as the existing system during the transitional period. After that period it would raise more than the present system. Thus after four or five years tax rates could be further reduced.

Detailed estimates were made by the Commission of the revenue the proposed system would have raised in 1964, had there been no transitional costs. These changes in brief: (in millions of dollars)

Corporation income tax	532
Personal income tax	−42
Gift and estate taxes	−143
Sales tax	−125
Total change	222

Because of the proposed integration of personal and corporation taxes and the move from gift and estate taxes to the taxation of gifts as income, these estimates must be interpreted carefully.

A large proportion of the increase in corporation tax collections would be borne by non-residents and would result from the withdrawal of both the dual rate of corporation tax and special industry concessions. The increase in corporation tax attributable to residents would be more than offset by the refunds of corporation tax to resident shareholders. Despite the full taxation of share gains, the weight of tax on corporate source income would be reduced for resident shareholders as a group.

Taxing gifts as income would result in more revenue being raised despite the abolition of gift and estate taxes as such.

The proposed new tax system also would have the effect of redistributing income in favour of those with low incomes. At present, the Commission said, some low income families are overtaxed because they do not benefit as much from government expenditures as other families with the same income. And some upper income families are not contributing enough through taxes to this income redistribution.

"We are firmly convinced that this redistribution is necessary if we are to achieve greater equality of opportunity for all Canadians and make it possible for those with little economic power to attain a decent standard of living," the Commission said.

"However, we are also convinced that the rates of tax which are applicable at any level of income should not be so high as to discourage initiative and thereby reduce the production of goods and services for Canadians."

The following table shows the number of taxpayers in each income class who would experience increases, decreases, and no changes in direct taxes (all personal and corporation income taxes and gift and estate taxes) if the Commission's recommendations were implemented:

MAIN PROPOSALS CANADIAN ROYAL COMMISSION

Comprehensive Income	Decreased by more than 15 per cent	Changed by less than 15 per cent	Increased by more than 15 per cent
Less than $ 5,000	2,713,328	1,685,259	370,048
$ 5,000 - $ 9,999	404,144	1,038,796	173,338
$ 10,000 - $ 14,999	5,269	125,901	37,960
$ 15,000 - $ 24,999	1,895	70,918	23,885
$ 25,000 or over	182	42,263	26,259
Total	3,124,818	2,963,137	631,490

The Commission was appointed in 1962 to make the widest possible inquiry into the Canadian tax system. Cost of the inquiry will be close to $ 3,500,000.

Although the Commission looked into every aspect of federal taxes, except tariffs, it did not deal directly with provincial or municipal taxation, except to reject proposals that home-owners be given credit for property taxes in computing federal income taxes.

Said the Commission:

"We hope Canadians will accept the challenge implicit in our recommendations. And there can be no doubt that our recommendations constitute a great challenge. Preconceived opinions about taxation are deeply and firmly held. Many will find it extremely difficult to take a new look at old questions. Because some facts cannot be readily ascertained, honest differences of opinion are inevitable. There is a danger that the debate about these minor factual questions will divert attention from the major issues.

"In the same way great damage could be done by the espousal of all the popular measures recommended and rejection of others—without appreciating that the politically attractive changes are only feasible as part of an integrated programme. These and many other hurdles have to be overcome if Canada is going to obtain the best possible tax system."

Chairman of the six-member Commission was Kenneth LeMesurier Carter, 60, of Toronto, a chartered accountant, a former Chairman of the Board of Governors of the Canadian Tax Foundation, and at the time of his appointment President of the Canadian Welfare Council.

Other Commissioners: J. Harvey Perry, York Mills, Ontario, former Director of the Canadian Tax Foundation, now Executive Director of the Canadian Bankers Association; A. Emile Beauvais, Quebec City, a Doctor in Financial Science at Laval University, and a past Governor of the Tax Foundation; Donald G. Grant, Halifax, a lawyer, President of the Nova Scotia Trust Company and director of several large Maritime firms; Mrs. Eleanor Milne, Winnipeg, active in the financial management of several organizations; and Charles E.S. Walls, Victoria, a farmer, Manager of the British Columbia Federation of Agriculture.

All members of the Commission signed the main Report. However, both Mr. Beauvais and Mr. Grant submitted minority reports, taking issue with several of the major and minor recommendations, particularly the taxation of all capital gains at progressive rates.

The Commission levelled these criticisms against Canada's existing tax system:

1. It does not afford fair treatment for all Canadians. People in essentially similar circumstances do not pay the same taxes. People in essentially different circumstances do not bear appropriately different tax burdens.

2. Canadians are less well off than they could be because there are fewer goods and services available than could be achieved with the more efficient use of labour, capital and natural resources. The present tax system has contributed to this situation.

3. Compliance and collection costs have been needlessly raised by duplication in federal and provincial administrations. Federal tax administration is not sufficiently shielded from political influence, and is too centralized for efficiency and convenience. Federal administrative and judicial appeal procedures are deficient.

4. The fiscal system has not been used as effectively as it could have been used to maintain full employment, contain inflation, and encourage Canadian ownership and control of Canadian industry.

5. Federal procedures used to obtain and analyze new ideas prior to the introduction of new tax legislation are inadequate—as are the procedures for hearing the views of taxpayers on proposed legislation.

"We are fully aware that these conclusions constitute a severe criticism of the present tax system," the Commissioners said. "They were not arrived at lightly nor are they the inevitable result of preconceived opinions. Our bias when we began our task was that the present system was basically sound and compared favourably with the systems of other countries.

"While we are still of the opinion that the present Canadian tax system is as good as most other systems, we are convinced that it falls far short of the attainable objectives.

"We therefore recommend many fundamental changes which, if adopted, would produce a complete transformation and, we believe, result in greater equity and efficiency.'

In designing the new tax system, the Commission sought to achieve several objectives —equity, protection of individual rights and liberties, economic growth and stability, the strengthening of Confederation. But some of these goals conflicted when specific proposals were being considered.

Whenever such conflicts arose that could not be compensated for by making adjustments in other features of the proposed system, or by recommending changes in other government policies, they were reconciled in favour of equity.

"We are convinced that preserving and developing the system by scrupulously fair taxes must override all other objectives," the Commission said.

At the same time, the Commission is convinced that the tax system proposed is both administratively workable and would increase the future output of the Canadian economy.

The Commission believes that taxes, to be equitable, should be allocated according to the ability to pay. This requires that individuals and families pay taxes that are proportionate to their discretionary economic power. And this in turn is defined as the power to command goods and services for personal use after meeting personal and family obligations and responsibilities.

Determining the relative discretionary economic power of individuals and families is partly a matter of judgment. The Commission has embodied these judgments in the proposed schedules of progressive tax rates, and in the concessionary tax credits and deductions provided to tax units with different family characteristics.

But to avoid capricious results, these rates and concessionary provisions must be applied to a tax base that measures the changes in each tax unit's total economic power.

This is the principle underlying the new comprehensive tax base. It simply measures all "income". But under the new tax system, income would be a much broader concept than "income" at present.

Said the Commission:

"If a man obtains increased command over goods and services for his personal satisfaction we do not believe it matters, from the point of view of taxation, whether he earned it through working, gained it through operating a business, received it because he held property, made it by selling property or was given it by a relative.

"Nor do we believe it matters whether the increased command over goods and services was in cash or in kind. Nor do we believe it matters whether the increase in economic power was expected or unexpected, whether it was a unique or recurrent event, whether the man suffered to get the increase in economic power or it fell into his lap without effort.

"All of these considerations should be ignored either because they are impossible to determine objectively in practice or because they are irrelevant in principle, or both.

"By adopting a base that measures changes in the power, whether exercised or not, to consume goods and services we obtain certainty, consistency and equity."

Taxing different kinds of gains differently opens many loopholes. It places great pressure on the development of tax minimization schemes. It also distorts the economy, for people are encouraged to do things that produce gains that are lightly taxed, and to avoid activities that result in gains that are heavily taxed. The shunned activities are often more productive.

The attempt to distinguish between ("income" gains and "capital" gains has also meant a great deal of uncertainty. No clear line of demarcation is possible.

The Commission's terms of reference required it to devise a tax system that would raise "sufficient" revenue—that is, about the same revenue as the present system. The Commission emphasized that if marginal rates are to be reduced, the tax base must be broadened, inefficient concessions must be replaced by equally effective concessions that have a lower revenue cost, and unnecessary concessions must be withdrawn.

The adoption of the comprehensive tax base can be looked upon as part of the price paid for a general reduction in tax rates.

Most employees already are taxed on a base that is even broader than the comprehensive tax base as the Commission would define it. For them, the proposal would involve no great changes. The tax base for most of those who depend primarily on other kinds of income would be greatly broadened.

The most contentious addition to the tax base would be realized capital gains. Under the Commission's proposals, there would be a lifetime exemption of $ 25,000 on gains realized from the sale of houses and farms. Property gains would be deemed to have been realized on leaving Canada, or on death (unless the property passed to a surviving spouse or dependent child).

"A dollar gained through the sale of a share, bond, or piece of real estate bestows exactly the same economic power as a dollar gained through employment or operating a business," said the Commission. "The equity principles we hold dictate that both should be taxed in exactly the same way. To tax the gain on the disposal of property more lightly than other kinds of gains or not at all would be grossly unfair.

"These radical reforms are advocated because equity can be achieved in no other way, because in our opinion there would be no adverse economic effects through their adoption when combined with our other proposed changes, and because they would simplify the tax system and reduce uncertainty.

"If the full taxation of property gains would result in dire economic circumstances or hopelessly complex administrative questions, some backing away from equity principles

could be justified. We are satisfied that neither justification holds."

The Commission said it must be recognized that taxation of capital gains would be only one part of a new system that would have greatly reduced marginal personal rates of tax, liberal new income-averaging provisions to soften the tax impact of income fluctuations, full credit to resident shareholders for Canadian corporation taxes, more efficient incentives for new and small business, loss provisions to remove any tax bias against risk-taking, and an increased tax concession to retirement savings.

"As one component of a package with these features, we can dismiss the claims that to tax capital gains would destroy initiative, reduce saving, and drive people out of the country."

But in addition, many other receipts—some now exempt from tax—would be added to the tax base. Included would be family allowances, noncash benefits provided by employers (such as the full market value of free or low cost meals or lodging), patronage dividends by consumer co-operatives, interest rebates from credit unions, life insurance policy dividends and the property income earned each year on policy reserves.

Also included in the new tax base would be all benefits paid under "income insurance" plans, including unemployment insurance, supplementary unemployment insurance, workmen's compensation, sickness and accident insurance and group life insurance. But contributions of both employees and employers would be deductible in computing their incomes.

(In recommending that government transfer payments such as unemployment insurance and workmen's compensation be taxed as income, the Commission emphasized that it is not prejudging the adequacy of these payments. It recommends that governments review the size of the benefits if they are brought into the tax base. The point is not that they are too big or too small, but that by failing to tax them some beneficiaries under these plans now are paying less tax than others with the same economic power. Exemptions and deductions from income provide no benefit to those who have no taxable income. The only way to help these people—the people who most need the help—is to increase government transfer payments.)

Gambling gains also would be added to taxable income. The Commission said gambling losses should be deductible against gambling gains but not against other income. Such gains are not now taxed unless the taxpayer makes a business of gambling.

Strike pay also would be taxed; the Commission regards it as an addition to income under an informal income-maintenance scheme. Union dues, of course, would still be deductible for tax purposes.

The estate and gift taxes would be abolished. But gifts and inheritances would be taxed to the recipient—as part of income—if they came from outside the family tax unit. Thus there would no longer be any tax on bequests to a widow from her husband. Each person would have a $ 5,000 lifetime exemption on such gifts and bequests, and in addition there would be annual exemptions of $ 250 for each individual, $ 500 for each married couple and $ 100 for each dependent child. In effect, most people would never pay tax on any gifts.

Having adopted the principle of taxing net gains in discretionary economic power, the Commission then tackled the problem of how to make allowance for non-discretionary spending—the outlays required to meet personal and family responsibilities.

Under the present tax system this is accomplished to a certain degree through exemptions—the $ 1,000 exemption for everyone,

the $ 1,000 additional exemption for a wife whose income does not exceed a certain amount, and the $ 300 exemption for each child qualified to receive family allowances. This arrangement would be substantially modified under the Commission's proposals. Replacing it would be a personal income tax rate schedule for individuals and another schedule for family income. In both cases the first-income bracket would be taxed at a zero rate. The zero-rate bracket would be $ 1,000 for individuals and $ 2,100 for families. These zero-rate brackets would have exactly the same effects as exemptions.

In addition, the costs of raising children—costs which usually are higher for the first than for subsequent children—would be recognized through tax credits. These would amount to $ 100 for the first child, and $ 60 for each additional child. For low and middle income families, the proposed tax credits would be more valuable than the present exemptions.

If both husband and wife were at work for more than 120 days a year, and if they had one or more children, they would be allowed to reduce their income taxes otherwise payable by $ 80. They would get an additional tax credit of $ 120 a year if their family included a child under 7 years old—to recognize the additional costs incurred by working mothers of preschool youngsters.

Following are the separate rate schedules recommended by the Commission:

RECOMMENDED RATE SCHEDULES

Taxable Income	Unattached Individuals		Family Units	
	Tax at Bottom of Bracket	Marginal Tax Rate on Income In Bracket	Tax at Bottom of Bracket	Marginal Tax Rate on Income In Bracket
	$	%	$	%
Less than $ 1,000	None	—	None	—
$ 1,000 - 1,500	None	12	None	—
1,500 - 2,000	60	15	None	—
2,000 - 2,100	135	17	None	—
2,100 - 3,000	152	17	None	13
3,000 - 4,000	305	20	117	16
4,000 - 5,000	505	22	277	18
5,000 - 6,000	725	23	457	19
6,000 - 8,000	955	24	647	20
8,000 - 10,000	1,435	26	1,047	21
10,000 - 12,000	1,955	28	1,467	22
12,000 - 15,000	2,515	30	1,907	24
15,000 - 20,000	3,415	32	2,627	27
20,000 - 25,000	5,015	35	3,977	31
25,000 - 30,000	6,765	37	5,527	35
30,000 - 40,000	8,615	39	7,277	38
40,000 - 50,000	12,515	42	11,077	42
50,000 - 60,000	16,715	44	15,277	44
60,000 - 80,000	21,115	46	19,677	46
80,000 - 100,000	30,315	49	28,877	49
Over 100,000	40,115	50	38,677	50

The way in which people would be affected by these changes would vary widely according to their individual circumstances.
Obviously, however, if a person's taxable income was not increased by switching to the comprehensive tax base, the lower rates would mean lower taxes. This in fact would be the case for almost all individuals and families whose income is strictly from wages and salaries.
Changes for this group are shown in the following table.

CHANGES IN TAX LIABILITIES UNDER THE PROPOSED TAX SYSTEM FOR AN UNATTACHED INDIVIDUAL AND A FAMILY UNIT WITH ONE INCOME RECIPIENT

Gross Employment Income		Status of Taxpayer						
		Unattached Individual	Married Couple					
			Number of Children					
			0	1	2	3	5	8
1500	Current Tax (1966 Rates)	51.	0.	0.	0.	0.	0.	0.
	Tax under our Proposals	49.	0.	0.	0.	0.	0.	0.
	Increase or Decrease in Tax	−3.	0.	0.	0.	0.	0.	0.
2000	Current Tax (1966 Rates)	115.	0.	0.	0.	0.	0.	0.
	Tax under our Proposals	119.	0.	0.	0.	0.	0.	0.
	Increase or Decrease in Tax	3.	0.	0.	0.	0.	0.	0.
2500	Current Tax (1966 Rates)	202.	51.	13.	0.	0.	0.	0.
	Tax under our Proposals	199.	36.	0.	0.	0.	0.	0.
	Increase or Decrease in Tax	−3.	−15.	−13.	0.	0.	0.	0.
3000	Current Tax (1966 Rates)	292.	115.	77.	38.	0.	0.	0.
	Tax under our Proposals	281.	99.	8.	0.	0.	0.	0.
	Increase or Decrease in Tax	−11.	−16.	−69.	−38.	0.	0.	0.
3500	Current Tax (1966 Rates)	394.	202.	148.	102.	64.	0.	0.
	Tax under our Proposals	374.	172.	84.	35.	0.	0.	0.
	Increase or Decrease in Tax	−20.	−30.	−64.	−67.	−64.	0.	0.
4000	Current Tax (1966 Rates)	499.	292.	238.	184.	130.	51.	0.
	Tax under our Proposals	471.	250.	161.	113.	65.	0.	0.
	Increase or Decrease in Tax	−28.	−42.	−77.	−71.	−65.	−51.	0.
5000	Current Tax (1966 Rates)	691.	499.	436.	373.	310.	202.	64.
	Tax under our Proposals	681.	421.	334.	287.	240.	147.	8.
	Increase or Decrease in Tax	−10.	−78.	−102.	−86.	−70.	−55.	−56.
6500	Current Tax (1966 Rates)	1018.	798.	732.	672.	615.	499.	310.
	Tax under our Proposals	1016.	698.	612.	567.	521.	430.	293.
	Increase or Decrease in Tax	−2.	−100.	−120.	−105.	−94.	−69.	−17.
8000	Current Tax (1966 Rates)	1384.	1128.	1062.	996.	930.	798.	615.
	Tax under our Proposals	1365.	989.	903.	858.	812.	722.	587.
	Increase or Decrease in Tax	−19.	−139.	−159.	−138.	−118.	−76.	−28.

(Following on page 210).

CHANGES IN TAX LIABILITIES UNDER THE PROPOSED TAX SYSTEM FOR AN UNATTACHED INDIVIDUAL AND A FAMILY UNIT WITH ONE INCOME RECIPIENT

Gross Employment income		Status of Taxpayer						
		Unattached Individual	Married Couple					
			Number of Children					
			0	1	2	3	5	8
10000	Current Tax (1966 Rates)	1940.	1644.	1566.	1488.	1410.	1254.	1040.
	Tax under our Proposals	1864.	1393.	1309.	1264.	1219.	1129.	997.
	Increase or Decrease in Tax	-76.	-251.	-257.	-224.	-191.	-125.	-43.
12000	Current Tax (1966 Rates)	2585.	2240.	2150.	2060.	1970.	1790.	1540.
	Tax under our Proposals	2400.	1817.	1733.	1688.	1644.	1556.	1427.
	Increase or Decrease in Tax	-185.	-423.	-417.	-372.	-326.	-234.	-113.
15000	Current Tax (1966 Rates)	3730.	3330.	3210.	3090.	2970.	2760.	2445.
	Tax under our Proposals	3265.	2507.	2424.	2382.	2339.	2253.	2128.
	Increase or Decrease in Tax	-465.	-823.	-786.	-708.	-631.	-507.	-317.
20000	Current Tax (1966 Rates)	5925.	5475.	5340.	5205.	5070.	4800.	4395.
	Tax under our Proposals	4839.	3828.	3748.	3707.	3667.	3586.	3465.
	Increase or Decrease in Tax	-1086.	-1647.	-1592.	-1498.	-1403.	-1214.	-930.
25000	Current Tax (1966 Rates)	8175.	7725.	7590.	7455.	7320.	7050.	6645.
	Tax under our Proposals	6572.	5356.	5279.	5241.	5203.	5128.	5016.
	Increase or Decrease in Tax	-1603.	-2369.	-2311.	-2214.	-2117.	-1922.	-1629.
30000	Current Tax (1966 Rates)	10620.	10120.	9970.	9820.	9670.	9370.	8920.
	Tax under our Proposals	8411.	7084.	7010.	6975.	6940.	6870.	6767.
	Increase or Decrease in Tax	-2209.	-3036.	-2960.	-2845.	-2730.	-2500.	-2153.
40000	Current Tax (1966 Rates)	15620.	15120.	14970.	14820.	14670.	14370.	13920.
	Tax under our Proposals	12300.	10868.	10795.	10763.	10730.	10665.	10568.
	Increase or Decrease in Tax	-3320.	-4252.	-4175.	-4057.	-3940.	-3705.	-3352.
50000	Current Tax (1966 Rates)	21065.	20515.	20350.	20185.	20020.	19690.	19195.
	Tax under our Proposals	16484.	15046.	14976.	14946.	14917.	14857.	14768.
	Increase or Decrease in Tax	-4581.	-5469.	-5374.	-5239.	-5103.	-4833.	-4427.
70000	Current Tax (1966 Rates)	32510.	31910.	31730.	31550.	31370.	31010.	30470.
	Tax under our Proposals	25462.	24024.	23957.	23930.	23903.	23850.	23769.
	Increase or Decrease in Tax	-7048.	-7886.	-7773.	-7620.	-7467.	-7160.	-6701.
100000	Current Tax (1966 Rates)	50955.	50305.	50110.	49915.	49720.	49330.	48745.
	Tax under our Proposals	39845.	38407.	38343.	38318.	38293.	38244.	38170.
	Increase or Decrease in Tax	-11110.	-11898.	-11767.	-11597.	-11427.	-11086.	-10575.
200000	Current Tax (1966 Rates)	119650.	118950.	118740.	118530.	118320.	117900.	117270.
	Tax under our Proposals	89840.	88402.	88338.	88314.	88290.	88242.	88170.
	Increase or Decrease in Tax	-29810.	-30548.	-30402.	-30216.	-30030.	-29658.	-29100.

It is important to note that this table shows changes in taxes only in comparison with personal income tax rates that were in effect prior to the Budget Speech of December 19, 1966.

The proposed "integration" of personal and corporation income taxes would result in all corporate source income for residents being taxed only once—and then at the rate applying to each individual shareholder.

Briefly, this system would work this way:

Resident shareholders in Canadian corporations would include in their tax bases their full share of the corporate income paid or allocated to them. The amount of this dividend or allocation would be "grossed-up" to include the income tax already collected from the corporation.

The resident shareholder (but not the non-resident) would calculate his income tax and then would deduct a tax credit equal to the income tax already paid by the corporation on his share of its income. If the tax credit exceeded his tax liability, he would get a refund.

For example, suppose a shareholder in a 30 per cent tax bracket received a $ 50 cash dividend from a corporation which had been taxed at 50 percent.

For tax purposes, this shareholder would gross-up the dividend and bring into income the full $ 100—his share of the corporations's profits before taxes. His tax on that $ 100 would be $ 30. From this he would deduct the tax of $ 50 already collected from the corporation. Thus there would be a refund of $ 20. The total cash received by the shareholder would therefore be $ 70 (the $ 20 refund plus the $ 50 dividend). At present, such a shareholder in the same tax bracket would have $ 45 in cash after paying tax on the dividend.

However, the benefit from integration would be partly offset in many cases by the taxation of realized share gains. Many of those who receive their income primarily from investments and have large capital gains would experience higher taxes despite integration.

From the Commission's estimates it is clear that most low and middle income shareholders would find their after-tax corporate source income (including capital gains) increased under these proposals.

The following table illustrates how taxpayers in some different situations would be affected by the integration system.

These calculations are based on three all-important assumptions:

1. The table deals only with those who receive all of their income from typical Canadian public companies.

2. Share gains are realized each year.

3. The taxable portion of the share gain is assumed to be equal to the cash dividend. And the cash dividend is assumed to be equal to one half of the corporation's after-tax profit. *(See tables on the pages 212 and 213).*

CHANGES IN TAX LIABILITIES UNDER THE PROPOSED TAX SYSTEM (INCLUDING TAXES PAID BY CORPORATIONS) FOR A TAX UNIT WITH INCOME FROM A TYPICAL PUBLIC COMPANY

Gross Corporate source Income		Status of Taypayer						
		Unattached Individual	Married Couple					
			Number of Children					
			0	1	2	3	5	8
1500	Current Tax (1966 Rates)	591.	591.	591.	591.	591.	591.	591.
	Tax under our Proposals	54.	0.	0.	0.	0.	0.	0.
	Increase or Decrease in Tax	-537.	-591.	-591.	-591.	-591.	-591.	-591.
2000	Current Tax (1966 Rates)	789.	789.	789.	789.	789.	789.	789.
	Tax under our Proposals	128.	0.	0.	0.	0.	0.	0.
	Increase or Decrease in Tax	-661.	-789.	-789.	-789.	-789.	-789.	-789.
2500	Current Tax (1966 Rates)	986.	986.	986.	986.	986.	986.	986.
	Tax under our Proposals	212.	46.	0.	0.	0.	0.	0.
	Increase or Decrease in Tax	-774.	-940.	-986.	-986.	-986.	-986.	-986.
3000	Current Tax (1966 Rates)	1183.	1183.	1183.	1183.	1183.	1183.	1183.
	Tax under our Proposals	297.	111.	21.	0.	0.	0.	0.
	Increase or Decrease in Tax	-886.	-1072.	-1162.	-1183.	-1183.	-1183.	-1183.
3500	Current Tax (1966 Rates)	1380.	1380.	1380.	1380.	1380.	1380.	1380.
	Tax under our Proposals	395.	189.	101.	52.	4.	0.	0.
	Increase or Decrease in Tax	-985.	-1191.	-1279.	-1328.	-1376.	-1380.	-1380.
4000	Current Tax (1966 Rates)	1577.	1577.	1577.	1577.	1577.	1577.	1577.
	Tax under our Proposals	495.	269.	181.	134.	87.	0.	0.
	Increase or Decrease in Tax	-1082.	-1308.	-1396.	-1443.	-1490.	-1577.	-1577.
5000	Current Tax (1966 Rates)	1971.	1971.	1971.	1971.	1971.	1971.	1971.
	Tax under our Proposals	714.	448.	361.	315.	269.	176.	37.
	Increase or Decrease in Tax	-1257.	-1523.	-1610.	-1656.	-1703.	-1795.	-1934.
6500	Current Tax (1966 Rates)	2571.	2563.	2563.	2563.	2563.	2563.	2563.
	Tax under our Proposals	1063.	737.	651.	606.	560.	469.	332.
	Increase or Decrease in Tax	-1508.	-1826.	-1911.	-1957.	-2002.	-2094.	-2230.
8000	Current Tax (1966 Rates)	3175.	3154.	3154.	3154.	3154.	3154.	3154.
	Tax under our Proposals	1423.	1037.	952.	907.	862.	772.	637.
	Increase or Decrease in Tax	-1752.	-2117.	-2202.	-2247.	-2292.	-2382.	-2517.
10000	Current Tax (1966 Rates)	3979.	3943.	3943.	3943.	3943.	3943.	3943.
	Tax under our Proposals	1942.	1457.	1372.	1328.	1284.	1195.	1063.
	Increase or Decrease in Tax	-2037.	-2486.	-2571.	-2615.	-2659.	-2747.	-2880.
12000	Current Tax (1966 Rates)	4784.	4744.	4732.	4731.	4731.	4731.	4731.
	Tax under our Proposals	2501.	1896.	1812.	1770.	1727.	1641.	1513.
	Increase or Decrease in Tax	-2283.	-2848.	-2920.	-2961.	-3004.	-3090.	-3218.

(Following on page 213).

CHANGES IN TAX LIABILITIES UNDER THE PROPOSED TAX SYSTEM (INCLUDING TAXES PAID BY CORPORATIONS) FOR A TAX UNIT WITH INCOME FROM A TYPICAL PUBLIC COMPANY

Gross Corporate source Income		Status of Taxpayer						
		Unattached Individual	Married Couple					
			Number of Children					
			0	1	2	3	5	8
15000	Current Tax (1966 Rates)	5991.	5951.	5939.	5927.	5915.	5914.	5914.
	Tax under our Proposals	3400.	2615.	2533.	2492.	2452.	2371.	2249.
	Increase or Decrease in Tax	−2591.	−3336.	−3406.	−3435.	−3463.	−3543.	−3665.
20000	Current Tax (1966 Rates)	8003.	7963.	7951.	7939.	7927.	7903.	7885.
	Tax under our Proposals	4999.	3964.	3884.	3846.	3808.	3733.	3620.
	Increase or Decrease in Tax	−3004.	−3999.	−4067.	−4092.	−4118.	−4170.	−4265.
25000	Current Tax (1966 Rates)	9976.	9974.	9962.	9950.	9938.	9914.	9878
	Tax under our Proposals	6748.	5512.	5435.	5400.	5365.	5296.	5191.
	Increase or Decrease in Tax	−3229.	−4463.	−4528.	−4550.	−4573.	−4619.	−4687.
30000	Current Tax (1966 Rates)	11948.	11948.	11948.	11948.	11948.	11926.	11890.
	Tax under our Proposals	8597.	7260.	7185.	7153.	7120.	7055.	6957.
	Increase or Decrease in Tax	−3351.	−4688.	−4762.	−4795.	−4828.	−4871.	−4933.
40000	Current Tax (1966 Rates)	15890.	15890.	15890.	15890.	15890.	15890.	15890.
	Tax under our Proposals	12496.	11058.	10986.	10956.	10927.	10867.	10778.
	Increase or Decrease in Tax	−3395.	−4832.	−4904.	−4934.	−4963.	−5023.	−5112.
50000	Current Tax (1966 Rates)	19833.	19833.	19833.	19833.	19833.	19833.	19833.
	Tax under our Proposals	16694.	15256.	15187.	15158.	15130.	15073.	14988.
	Increase or Decrease in Tax	−3139.	−4577.	−4646.	−4674.	−4703.	−4759.	−4844.
70000	Current Tax (1966 Rates)	28155.	27755.	27718.	27718.	27718.	27718.	27718.
	Tax under our Proposals	25692.	24254.	24187.	24160.	24133.	24080.	23999.
	Increase or Decrease in Tax	−2463.	−3501.	−3531.	−3558.	−3584.	−3638.	−3719.
100000	Current Tax (1966 Rates)	41398.	40948.	40813.	40678.	40543.	40273.	39868.
	Tax under our Proposals	40091.	38653.	38588.	38564.	38540.	38492.	38420.
	Increase or Decrease in Tax	−1308.	−2296.	−2225.	−2114.	−2003.	−1781.	−1448.
200000	Current Tax (1966 Rates)	86586.	86086.	85936.	85786.	85636.	85336.	84886.
	Tax under our Proposals	90090.	88652.	88588.	88564.	88540.	88492.	88420.
	Increase or Decrease in Tax	3504.	2566.	2652.	2778.	2904.	3156.	3534.
350000	Current Tax (1966 Rates)	156767.	156167.	155987.	155807.	155627.	155267.	154727.
	Tax under our Proposals	165090.	163652.	163588.	163564.	163540.	163492.	163420.
	Increase or Decrease in Tax	8323.	7485.	7601.	7757.	7913.	8225.	8693.
600000	Current Tax (1966 Rates)	277024.	276374.	276179.	275984.	275789.	275399.	274814.
	Tax under our Proposals	290090.	288652.	288588.	288564.	288540.	288492.	288420.
	Increase or Decrease in Tax	13066.	12278.	12409.	12580.	12751.	13093.	13606.
1000000	Current Tax (1966 Rates)	474861.	474161.	473951.	473741.	473531.	473111.	472481.
	Tax under our Proposals	490090.	488652.	488588.	488564.	488540.	488492.	488420.
	Increase or Decrease in Tax	15229.	14491.	14637.	14823.	15009.	15381.	15939.

The Commission analyzed the effects the proposed new tax system would have on the volume and allocation of saving and investment. It is satisfied that despite the major increase in corporation tax collections and the substantial increase in the weight of tax on many high income individuals and families, total domestic saving would not be reduced.

By adopting a more neutral tax system the allocation of capital would be much improved, with the result that future production would be increased without forcing Canadians to save more, and without Canada relying more heavily on foreign saving.

The Commission said that the low rate of tax on the first $ 35,000 of corporation income, percentage depletion for the extractive industries, the three-year exemption for new mines, and the failure to tax adequately the business income of life insurance companies, are extremely costly in terms of revenue and are inefficient incentives.

It believes that the first one should be replaced by a more efficient incentive, the next two should be withdrawn and life insurance companies should be taxed like other businesses. The revenue saving could be used to lower taxes on marginal investments in other industries that have higher expected rates of return.

By allowing mining and petroleum companies to deduct all of their costs before paying any tax, and by giving resident shareholders of the companies full credit for the corporation tax, the impact of the removal of the concessions would be mitigated. In fact, the immediate write-off of costs would mean that companies with substantial new investment would continue to pay little or no tax. In particular, most of the smaller companies would not be affected by the withdrawal of depletion and the three-year exemption for new mines.

By allowing the deduction of business losses that now are disallowed, and by allowing new and small businesses to write off their capital costs more rapidly, the biases of the market against some companies would be compensated for more effectively.

By giving residents full credit for Canadian corporation tax collections the shares of Canadian companies would be a much more attractive investment than they now are to most Canadians, and to the institutions through which much of Canada's personal saving is channeled.

The Commission expects that, despite the full taxation of share gains, the prices of Canadian equities would rise. This would encourage a more rapid rate of capital investment by most Canadian companies that now do not benefit from special industry tax concessions. It would also encourage non-resident-controlled Canadian subsidiaries to offer shares to Canadians.

Should Canadians want greater increases in the rate of economic growth, the Commission recommends changes in the "mix" of monetary, fiscal, trade and exchange rate policies.

The Commission's second choice is the adoption of a system of investment tax credits and less stringent limitations on deductions for Registered Retirement Income Plans. The Commission emphasizes that it is unnecessary to reduce the progressiveness of the tax system to encourage more saving, when the same result could be obtained in other ways that would not reduce the fairness of the system.

Press Release

DER AUFBAU EINES EUROPÄISCHEN KAPITALMARKTS:

DIE STEUERLICHE HINDERNISSE

Die EWG Kommission hat eine Gruppe unabhängiger Sachverständigen damit beauftragt, die Gesamtheit der Fragen zu untersuchen, die sich aus der Verwirklichung des Vertrages von Rom für die Funktionsfähigkeit der europäischen Kapitalmärkte ergeben. Der Bericht ist November 1966 abgeschlossen. Wir publizieren den Text des Kapitels 14, das über die steuerlichen Hindernisse handelt.

BEMERKUNG DER SCHRIFTLEITUNG

1. Gegenstand dieses Kapitels ist ein Gesamtüberblick über diejenigen Änderungen der Steuersysteme, die die Entwicklung und das Funktionieren eines Kapitalmarktes wirklich europäischen Ausmaßes fördern könnten. Nach einer kurzen Darstellung der Grundsätze, von denen sich die Arbeitsgruppe leiten ließ, werden die zur Zeit noch bestehenden Behinderungen beschrieben und Wege zur Beseitigung der größten Hindernisse aufgezeigt.

I. ZIELSETZUNG

2. Die Besteuerung soll grundsätzlich so angepaßt werden, daß ihre Wirkungen neutral sind, d.h. daß sie der Schaffung binnenmarktähnlicher Verhältnisse im Kapitalverkehr der Gemeinschaft nicht mehr entgegenstehen. Dazu müssen im wesentlichen drei Bedingungen erfüllt werden, von denen sich die beiden ersten auf das reibungslose Funktionieren der einzelnen Marktbereiche und die dritte auf deren Gleichgewicht beziehen.

3. Erstens sollte die Besteuerung die Wahl des Ortes der Anlage oder des Geschäftes nicht beeinflussen. Diese Bedingung ergibt sich unmittelbar aus der angestrebten Marktgröße: Ein europäischer Markt ist offensichtlich größer als ein einzelner nationaler Markt.

4. Zum zweiten sollte die Besteuerung keinen Einfluß auf die Wahl des Anlegers zwischen der Direktanlage und der Inanspruchnahme eines Finanzinstituts haben. In mehreren Mitgliedstaaten wird diese zweite Bedingung selbst bei inländischen Finanzgeschäften gegenwärtig nur sehr unvollständig erfüllt. Für das reibungslose Funktionieren eines reinen Inlandsmarktes kann das nur ein geringes Hindernis sein, sofern das anlagesuchende Sparkapital über die Anlagemöglichkeiten und die Funktionsweise des Kapitalmarktes hinreichend unterrichtet ist. In der Möglichkeit, spezialisierte Finanzinstitute in Anspruch zu nehmen, sieht die Arbeitsgruppe dagegen eine grundlegende Voraussetzung für den Zugang breiter Sparerschichten zum Kapitalmarkt und vor allem zu Kapitalanlagen im Ausland, was der Bedingung der Neutralität ihre Bedeutung verleiht.

5. Zum Zeitpunkt der Verschmelzung der Kapitalmärkte müßte drittens die Besteuerung in den einzelnen Mitgliedstaaten dieselben Anreize für die relative Entwicklung

der einzelnen Anlagearten und Finanzierungsmöglichkeiten bieten. In der Zwischenzeit müßte nach Möglichkeit darauf hingewirkt werden, die Besteuerungsunterschiede zwischen den Mitgliedstaaten abzubauen.

Die Arbeitsgruppe beabsichtigt nicht sich für eine steuerliche Gleichbehandlung aller Anlagearten einzusetzen. Sie läßt Unterschiede in der Besteuerung gelten, mit denen die eine oder andere Anlageform gefördert werden soll, um unter den einzelnen Anlagearten ein als wirtschaftlich sinnvoll angesehenes Verhältnis herzustellen (z.B. eine steuerliche Begünstigung langfristiger Kapitalanlagen, um einen allzu großen Anteil der liquiden Sparformen einzudämmen; steuerliche Begünstigung des Aktiensparens, wenn das Angebot an Beteiligungskapital offenbar unzureichend ist).

Die Arbeitsgruppe hält es jedoch für wünschenswert, daß die Mitgliedstaaten schließlich generell die gleichen Anreize für gleiche Anlage- und Finanzierungsarten bieten. Diese Forderung ist kein Nahziel. Die Ausgangssituation ist in den einzelnen Ländern sehr verschieden, und deshalb erscheinen Unterschiede bei den steuerlichen Anreizen unter den gegenwärtigen Umständen mit dem reibungslosen Funktionieren eines internationalen Kapitalmarktes nicht unvereinbar.

6. Soweit diese unterschiedlichen Steuerbegünstigungen für einen längeren Zeitraum gedacht sind, beeinträchtigen sie den Kapitalmarkt nicht mehr als das von einem Land zum anderen unterschiedliche Anlageinteresse der Sparer und Unternehmen. Hingegen könnte eine Änderung der steuerlichen Anreize den Kapitalmarkt eines Landes stören, weil dadurch die Struktur des Kapitalangebots oder der Nachfrage plötzlich durch neue Faktoren beeinflußt wird.

Von den Staaten ist wohl erst nach einer entsprechenden Vereinbarung zu erwarten, daß sie diese steuerlichen Anreize nicht mehr einseitig ändern, was praktisch eine einheitliche Haltung in dieser Sache voraussetzt. Bis dahin könnten sich die Mitgliedstaaten nämlich – wie bisher – auf die Verfolgung konjunktureller, struktureller oder sozialer Ziele berufen.

II. DIE DERZEITIGEN HINDERNISSE

7. Die genannten Bedingungen können zur Zeit aus folgenden Gründen nicht erfüllt werden:

- Doppelbesteuerung,
- Begünstigung von Kapitalanlagen im Lande des steuerlichen Wohnsitzes oder umgekehrt Sonderbesteuerung nur für einige Mitgliedstaaten,
- von Land zu Land unterschiedliche Behandlung der Kapitaleinkünfte, die von beschränkt Steuerpflichtigen oder den Steuerbehörden nicht bekannten Personen bezogen werden.

Diese Hindernisse werden in diesem Abschnitt allgemein dargestellt, um einen Gesamtüberblick über die steuerlichen Kapitalmarktprobleme zu geben. Lösungsvorschläge für die wichtigsten Probleme werden in den folgenden Abschnitten besprochen.

A. DIE DOPPELBESTEUERUNG

a) Die internationale Doppelbesteuerung

8. Bei einer bestimmten Anlageart kann der Unterschied zwischen dem Bruttoertrag (vor den Steuern) und dem Nettoertrag (nach den Steuern), selbst wenn man die von Land zu Land unterschiedlichen Einkommen- bzw. Körperschaftsteuersätze außer acht läßt, je nach dem Anlageland mehr oder

weniger groß sein, weil die Steuern, wenn das Anlageland (Einkommensquelle) nicht der steuerliche Wohnsitz des Einkommensbeziehers ist, in zwei Ländern erhoben werden und sich bei dem Einkommensbezieher somit kumulieren. Soweit die Kapitalanlage wegen der Rendite erfolgt, führt diese Doppelbesteuerung zu einer Bevorzugung von Kapitalanlagen im Lande des steuerlichen Wohnsitzes des Einkommensbeziehers.

Eine Doppelbesteuerung ist bei direkten und bei indirekten Steuern möglich. Bei den indirekten Steuern ist der Satz in der Regel niedriger als bei den direkten Steuern; da sie aber vielfach auf das Kapital und nicht auf das Einkommen erhoben werden, kann ihre Auswirkung auf die Rendite nicht vernachlässigt werden.

Die internationale Doppelbesteuerung würde zwischen Staaten vermieden werden, die für die gleichartigen Steuern eine einheitliche Besteuerung in einem der beiden Länder vereinbaren würden, wobei folgende Alternativen bestehen (1):

- bei der Einkommen- und Körperschaftsteuer: (Wohn-) Sitzland des Empfängers oder Land der Quelle,
- bei den Vermögensteuern: (Wohn-) Sitzland oder Land, in dem sich die Vermögensteile tatsächlich befinden,
- bei den indirekten Steuern: Bestimmungsland (Verbrauchsland) oder Ursprungsland (Produktionsland).

Würden die Mitgliedstaaten beschließen, bei der Besteuerung einheitliche Grundsätze anzuwenden, so gäbe es, geht man nur von den Bedingungen für ein reibungsloses Funktionieren des Kapitalmarktes aus, kein gewichtiges Argument für eine bestimmte Alternative; entscheidend wären dann andere Argumente, wie steuerliche oder haushaltspolitische Überlegungen.

Die Anwendung einheitlicher Grundsätze zur ausschließlichen Besteuerung der Einkünfte in einem einzigen Land wäre eine ideale Lösung zur Vermeidung der Doppelbesteuerung von Auslandsanlagen. Nach Ansicht der Sachverständigengruppe ist diese Lösung jedoch, betrachtet man sie nur unter dem Gesichtspunkt der Zielsetzungen der Kapitalmarktpolitik, nicht die einzig befriedigende. Es würde genügen, die Auswirkungen der Doppelbesteuerung beim Anleger zu neutralisieren, wenn die im Ausland gezahlten Steuern erstattungsfähig oder auf die Steuerschuld im Lande des Wohnsitzes voll anrechenbar sind.

b) Die Doppelbesteuerung bei Anlagen über ein Finanzinstitut

9. Die Rendite einer Anlage kann davon abhängen, ob diese direkt oder unter Inanspruchnahme eines Finanzinstituts (unabhängig von den dadurch entstehenden Kosten) vorgenommen wurde, wenn zu den Steuern bei Direktanlagen noch Steuern beim Finanzinstitut hinzukommen und diese für den Anleger weder erstattungsfähig noch anrechenbar sind.

In den meisten Mitgliedstaaten der Gemeinschaft gibt es Anlagearten der zweiten Art, die von jeder Nachbesteuerung ganz (oder sehr weitgehend) frei sind, aber meist nach nationalen Überlegungen geschaffen wurden und deshalb oft den Nachteil der internationalen Doppelbesteuerung von Auslandsanlagen dann nicht vermeiden, wenn die Anlagen nicht in dem Land vorgenommen werden, in dem der Anleger seiner Wohnsitz hat und vor allen dann, wenn der Kapitalanleger seinen steuerlichen Wohnsitz in einem anderen Land als das Finanzinstitut hat.

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(1) Nach der Klassifizierung des Steuer- und Finanzausschusses, Bericht des Steuer- und Finanzausschusses, 1962, S. 76

c) Die internationalen Doppelbesteuerungsabkommen

10. Selbst unter den Mitgliedstaaten der Gemeinschaft ist noch in zahlreichen Fällen eine Doppelbesteuerung möglich, teils weil Abkommen noch fehlen (Italien-Luxemburg, Luxemburg-Niederlande) oder weil die Abkommen sich nicht auf die Kapitalerträge beziehen (Belgien-Niederlande), teils weil einige sehr alte Abkommen den heutigen Steuersystemen nicht mehr entsprechen.
Ausserdem gehen die geltenden bilateralen Abkommen von verschiedenen, mitunter sogar entgegengesetzten Grundsätzen aus. Deshalb streben sie auch auf ganz verschiedenen Wegen eine Ausschaltung der Doppelbesteuerung an. Zudem sind einige Verfahren zur Anwendung der Abkommen so kompliziert, dass mancher Anleger davon abgehalten wird, sein Geld im Ausland zu investieren.
Die ideale Lösung zur Beseitigung der zwischen den Mitgliedstaaten immer noch bestehenden Doppelbesteuerung wäre wohl der Abschluss eines multilateralen Abkommens; der Abschluss eines multilateralen Abkommens in der Art des Musterabkommens der OECD wird übrigens bereits geprüft.
Soweit die laufenden Arbeiten auf diesem Gebiet nicht so bald abgeschlossen werden, wäre es vielleicht zweckmässig, zumindest eine Übergangslösung des Problems der Doppelbesteuerung im Rahmen bilateraler Abkommen darin zu suchen, dass das Abkommensnetz ergänzt wird und die bereits bestehenden Abkommen so verbessert werden, dass das Nebeneinanderbestehen zu unterschiedlicher Grundsätze und Verfahren verschwindet. In den Abschnitten III, IV und V dieses Kapitels werden praktische Vorschläge für die multilateralen und bilateralen Abkommen zur Diskussion gestellt.

Einseitige Maßnahmen der Staaten können die durch die Doppelbesteuerung entstehende Benachteiligung ihrer Gebietsansässigen ausgleichen: In manchen Staaten wird in Ermangelung eines Abkommens bereits eine – zumindest teilweise – Anrechnung der im Ausland vorgenommenen Abzüge durchgeführt.

B. STEUERVERGÜNSTIGUNG ODER -BELASTUNG VON KAPITALANLAGEN IN BESTIMMTEN LÄNDERN

a) Gewährung von Steuervergünstigungen für Kapitalanlagen im Wohnsitzland

11. Werden Steuervergünstigungen nur für Kapitalanlagen im Wohnsitzland gewährt, so steht dies schon dem Begriff nach der angestrebten Steuerneutralität entgegen. Dagegen besteht kein Anreiz für Kapitalanlagen in einem bestimmten Land, wenn die Steuervergünstigung jedem Anleger ohne Rücksicht auf seinen steuerlichen Wohnsitz gewährt wird, denn dann handelt es sich um eine Steuervergünstigung für den Kapitalnehmer. Die Steuervergünstigung hat ebenfalls keinen Einfluß auf die Wahl des Anlagelandes, wenn sie von dem betreffenden Staat an Personen gewährt wird, die dort ihren steuerlichen Wohnsitz haben, und wenn dabei keine Bedingungen hinsichtlich des Landes gestellt werden, in dem die Anlage vorgenommen wird.

b) Höhere Steuerbelastung von Kapitalanlagen oder Finanzierungsarten in bestimmten Ländern

Erhebt ein Land eine Steuer, für die es in anderen Ländern keine entsprechende Belastung gibt oder ist bei gleicher Steuerart der Steuersatz eines bestimmten Landes höher als in den anderen Ländern, so kann dies dort

bestimmte Finanzierungsarten gegenüber anderen Ländern verteuern oder die Kosten bestimmter Finanzgeschäfte erhöhen. Bei den indirekten Steuern auf die Kapitalaufnahme und den Kapitalverkehr ist dies häufig der Fall. Von den direkten Steuern sind vor allem bestimmte Zedularsteuern (die einzelne Einkommensarten unabhängig vom Gesamteinkommen eines Steuerpflichtigen belasten) betroffen. Einige Unterschiede in der Besteuerung der Gesellschaften könnten dieselbe Wirkung haben, doch würde eine Behandlung dieses Problems den Rahmen dieser Untersuchung überschreiten.

C. VON LAND ZU LAND UNTERSCHIEDLICHE BEHANDLUNG DER KAPITALERTRÄGE VON GEBIETSFREMDEN ODER VON PERSONEN, WELCHE IHRE ANONYMITÄT WAHREN

12. Werden in dem Land, in dem sich die Quelle dieser Kapitalerträge befindet, Dividenden oder Zinsen an einen Gebietsfremden gezahlt, der sich auf kein Doppelbesteuerungsabkommen berufen kann, so wird die Steuerbehörde des Landes, in dem der Bezieher dieser Einkünfte seinen Wohnsitz hat, zur Zeit davon üblicherweise nicht benachrichtigt. Da die Gebietsfremden in zahlreichen Ländern nur einer begrenzten Steuerpflicht unterliegen und nur mit dem Quellenabzug zu einem festen Satz besteuert werden, ist es dem gebietsfremden Bezieher von Kapitaleinkünften häufig möglich, sich einseitig jeder progressiven Steuer zu entziehen, indem er diese Einkünfte im Land der Quelle bezieht, ohne sie im Land seines Wohnsitzes zu versteuern; auf diese Weise wird er lediglich im Land der Quelle besteuert, und zwar zu dem Pauschalsatz, welchen dieses Land gegenüber Gebietsfremden anwendet, die nicht unter ein internationales Doppelbesteuerungsabkommen fallen.

In bestimmten Ländern können sogar die eigenen Gebietsansässigen der Einkommensteuerprogression bei bestimmten Arten von Kapitalerträgen deswegen entgehen, weil diese Einkünfte nur einem Quellenabzug unterworfen werden, mit dem sämtlich die Steuer abgegolten ist. Andere Länder, in denen zwar de jure der Grundsatz des Quellenabzugs mit befreiender Wirkung nicht gilt, nehmen einen Quellenabzug vor, welcher de facto die gleiche befreiende Wirkung haben kann, da die diesem Abzug unterworfenen Personen der Steuerbehörde nicht namentlich genannt werden. Andere Länder schließlich unterwerfen die Zinszahlungen keinem Quellenabzug und verlangen auch nicht, daß die Bezieher dieser Einkünfte den Steuerbehörden namentlich mitgeteilt werden.

Diese Möglichkeiten, der Einkommensteuerprogression bei bestimmten Kapitalerträgen zu entgehen, üben eine offensichtliche Anziehungskraft auf Personen aus, deren Einkommenspitze in ihrem Wohnsitzland mit einem Satz besteuert wird, der über dem betreffenden Satz für den Quellenabzug liegt. Sie können auch für Personen von Interesse sein, bei denen dieser Satz niedriger als der Quellenabzug ist, wenn es sich dabei um Auslandserträge handelt, die der Doppelbesteuerung nicht vollständig entgehen würden, weil kein befriedigendes Doppelbesteuerungsabkommen besteht.

Diese von Land zu Land unterschiedliche steuerliche Behandlung der Kapitalerträge von Gebietsfremden, die sich nicht auf ein Doppelbesteuerungsabkommen berufen können, oder – in Ländern, in denen dieses möglich ist – von Personen, welche ihre Anonymität wahren, kann in bestimmten Marktsituationen einen Einfluß auf die Kapitalkosten und somit auf die Entwicklung der verschiedenen Finanzierungsformen ausüben. Um diese Auswirkungen zu ver-

meiden, die der Forderung nach einem erweiterten und funktionsfähigen europäischen Kapitalmarkt widersprechen würden, ist innerhalb der Gemeinschaft eine stärkere Harmonisierung der Besteuerungs- und Kontrollsysteme erforderlich. Die Sachverständigengruppe vertritt die Auffassung, daß diese Harmonisierung bei Anlagen in Rentenpapieren besonders dringlich ist. Für die Wahl einer Anlage in Aktien spielen die unmittelbaren Ertragserwartungen eine weniger entscheidende Rolle als bei Anlagen in Rentenpapieren.

13. Die Tabellen B und E des Anhangs geben den Steuersatz für die Spitze des Einkommens an, von dem ab es für den Kapitalanleger interessant wird, sich der Progression der persönlichen Einkommensteuer zu entziehen, in dem er den die persönliche Einkommensteuer abgeltenden Quellenabzug zahlt oder die Einkünfte aus Aktien und Obligationen in einem Land bezieht, in dem er seine Anonymität gegenüber der Steuerbehörde seines Wohnsitzes wahren kann. Die Tabellen berücksichtigen die Auswirkung der internationalen Doppelbesteuerungsabkommen, die in bestimmten Ländern auch ohne Abkommen zugelassene Anrechnung von Auslandssteuern und die in bestimmten Ländern gewährten Steuergutschriften (credit d'impôts). Diese Tabellen zeigen, unter welchen Voraussetzungen es von Interesse sein kann, sich der progressiven persönlichen Einkommensteuer zu entziehen; sie sagen nichts darüber aus, ob ein Anreiz besteht, eine bestimmte Anlage eher in einem Lande als in einem anderen vorzunehmen.

III. ÄNDERUNG DER DIREKTEN BESTEUERUNG BEI KAPITALANLAGEN NATÜRLICHER PERSONEN

14. Der Entwicklung eines echten internationalen Marktes für Direktanlagen natürlicher Personen stehen vor allem zwei der genannten Hindernisse entgegen:

- Doppelbesteuerung der Einkommen,
- Gewährung von Steuervergünstigungen nur für Kapitalanlagen im Wohnsitzland.

Die Sachverständigengruppe beschäftigte sich vor allem mit Aktien und Anleihen, da diese Anlageformen für Privatleute eine große Bedeutung haben und da bei diesen Anlagen steuerliche Überlegungen für die Wahl des Anlagelandes entscheidend sein können.

Die Sachverständigengruppe hat sich ferner auf die Prüfung von Einkommensteuerfragen beschränkt. Sie hielt es weder für notwendig noch überhaupt für möglich, beim jetzigen Stand die Besteuerung des Kapitalzuwachses, des Vermögens und der Erbschaften eingehend zu untersuchen. Diese Steuern können ähnliche Probleme aufwerfen wie die Einkommensteuer, und es ist wahrscheinlich, daß man bei den Lösungen dieser besonderen Probleme von den gleichen Grundsätzen ausgehen wird.

A. AKTIENBESITZ NATÜRLICHER PERSONEN

a) Die Doppelbesteuerung des Einkommens

15. Die Ausschüttung einer Dividende an eine natürliche Person mit Wohnsitz in einem anderen Lande als dem des Sitzes der ausschüttenden Gesellschaft kann, wenn die Dividende im Lande des Gesellschaftssitzes gezahlt wird, zur Doppelbesteuerung führen, und zwar durch einen Quellensteuerabzug im Lande des Gesellschaftssitzes und die

Erhebung der Einkommensteuer des Aktionärs im Lande seines steuerlichen Wohnsitzes. Bezieht der Aktionär die Dividende im Wohnsitzland, dann kann dies zu einem Steuerabzug durch die Zahlstelle führen. Dieser Steuerabzug ist eine Vorauszahlung auf die Einkommensteuer und grundsätzlich voll anrechenbar; eine etwaige Überzahlung wird erstattet. Zur Vermeidung solcher Doppelbesteuerungsfälle gibt es eine ganze Reihe steuertechnischer Möglichkeiten.

16. Die Mitgliedstaaten könnten vereinbaren, das Einkommen nur in einem Lande zu besteuern: Steuerabzug im Lande des Gesellschaftssitzes als praktisch endgültige Steuer und Verzicht auf die Einkommensteuer im Wohnsitzland oder aber ausschließliche Besteuerung im Wohnsitzland.
Die erste Lösung erscheint nur als Wahlmöglichkeit für den Aktionär akzeptabel; gleichzeitig wäre ein anderes Verfahren für Aktionäre einzuführen, deren Einkommenspitze zu einem Satz besteuert wird, der unter dem ausländischen Steuerabzug liegt, damit diese Personen nicht benachteiligt werden und nicht darauf verzichten, ihr Kapital im Ausland anzulegen.
Wird der Kapitalertrag dagegen nur im Lande des Aktionärs besteuert, so bestehen unter dem besonderen Blickwinkel dieser Untersuchung keinerlei Bedenken der Sachverständigengruppe; diese Besteuerung kann technisch durch die Nichterhebung des Steuerabzugs beim ausländischen Aktionär oder durch Erstattung der abgezogenen Steuern vorgenommen werden. Bei der Nichterhebung wird vermieden, daß dem Aktionär die Erträge in zwei Teilbeträgen zufließen. Sie kann aber eine Tür zur Steuerflucht öffnen, wenn sie nicht mit einer verstärkten Zusammenarbeit der Steuerverwaltungen der Mitgliedstaaten einhergeht, die sich die Namen der Aktionäre gegenseitig mitteilen müßten. Nach dem gegenwärtig zwischen einigen Mitgliedstaaten praktizierten Verfahren erfolgt die Erstattung dann, wenn der Aktionär nachweist, daß er das entsprechende Einkommen der Steuerverwaltung seines Landes mitgeteilt hat.

17. Staaten, die Doppelbesteuerungsabkommen schließen, könnten es vorziehen, die Steuereinnahmen zu teilen, und zwar durch die eines Steuerabzugs im Quellenland und die systematische Anrechnung dieses Steuerabzugs im Wohnsitzland. Bezahlt der Einkommensbezieher überhaupt keine Steuer oder ist diese geringer als der abgezogene Betrag, wäre die Differenz zu erstatten.
Diese Lösung ist eine Verbesserung der bereits weit verbreiteten Praxis zur Vermeidung der Doppelbesteuerung, bei der Besteuerung der Kapitalerträge im Wohnsitzland die finanziellen Interessen des Quellenstaates zu wahren oder, mit anderen Worten, das Steueraufkommen aus diesen Einkünften zwischen den beiden Staaten zu teilen; das Ergebnis dieser Teilung hängt vom Satz der Quellensteuer und von der Höhe der Steuer ab, die der Einkommensbezieher im Wohnsitzland endgültig zu erbringen hat. Um eine ausgewogene Teilung zu erreichen, wird in den geltenden Abkommen, die diesen Weg wählen, im Verkehr der Unterzeichnerstaaten untereinander häufig ein niedrigerer Steuersatz festgelegt als er für solche Ausländer gilt, die sich auf ein Abkommen nicht berufen können oder wollen. Zu diesem ermäßigten Steuersatz gelangt man entweder durch die teilweise Erstattung des zunächst zum normalen Satz vorgenommenen Steuerabzugs oder durch einen von vornherein ermäßigten Satz.

18. Wie die Staaten die Steuereinnahmen untereinander aufteilen, wirkt sich auf den Kapitalmarkt kaum aus. Das reibungslose

Funktionieren erfordert dagegen, daß jener im Lande des Gesellschaftssitzes nicht erstattungsfähige Steuerabzug im Wohnsitzland voll anrechenbar ist und sogar erstattet werden kann, falls er die Einkommensteuerschuld in diesem Land übersteigt.

Dieses Ziel wird gegenwärtig nur unvollkommen erreicht. Einige Länder gestatten überhaupt keine Anrechnung von Auslandsabzügen. Auch in den übrigen Ländern ist oft nur eine teilweise Anrechnung möglich. Zahlreiche Länder erlauben die Anrechnung von Auslandsabzügen nur bis zur Höhe der inländischen Steuerschuld für den Anteil der Auslandsdividenden am Gesamteinkommen; damit werden die Auslandsanlagen solcher Personen benachteiligt, die zu einem unter dem Auslandsabzug liegenden Satz besteuert werden. Andere Länder wieder nehmen die Anrechnung von Auslandsabzügen ohne Rücksicht auf den inländischen Einkommensteuersatz der Aktionäre, jedoch nur bis zur Höhe des Steuersatzes vor, den sie gegenüber Auslandsaktionären ihrer inländischen Gesellschaften anwenden.

19. Abgesehen von den verwaltungsmäßigen Schwierigkeiten, die mit solchen Verfahren verbunden sein können, hätte die Sachverständigengruppe nichts dagegen einzuwenden, wenn die Mitgliedstaaten vereinbarten, im Land des Gesellschaftssitzes einen Steuerabzug für ausländische Aktionäre beizubehalten, wenn der Abzug auf die Steuerschuld des Aktionärs im Wohnsitzlande voll anrechenbar ist und eine eventuelle Überzahlung zurückerstattet werden kann. Diese Lösung enthielte den heute unzulässigen Grundsatz einer eventuellen Rückerstattung des Steuerabzugs durch das Wohnsitzland; sie könnte zu zwischenstaatlichen Ausgleichszahlungen führen, soweit die Staaten eine Erstattung von Steuern ablehnen, die ihnen nicht zugeflossen sind. Weil ein solcher Steuerabzug für den Aktionär immer das Wesen einer Steuervorauszahlung hat, dürfte er – wie hoch auch immer der Steuersatz festgesetzt wird – auf die Wahl des Anlagelandes kaum einen Einfluß besitzen. Trotzdem wäre es wünschenswert, wenn der Steuersatz in allen Ländern gleich wäre und dem Steuersatz für Aktionäre mit Wohnsitz im Lande des Gesellschaftssitzes entspräche. Dadurch würden nämlich Ertragsvergleiche erleichtert werden, was dazu beitragen würde, daß die Besteuerung bei der Wahl des Anlageortes noch mehr an Bedeutung verliert.

b) Die Beschränkung von Steuervergünstigungen auf Anlagen im Wohnsitzland

20. Seit einiger Zeit werfen einige Länder durch bestimmte Steuertechniken, die geeignet sind, den internationalen Kapitalverkehr zu behindern, besondere Probleme auf. So gewährt Belgien Gebietsansässigen nur für Dividenden inländischer Gesellschaften eine Steuergutschrift, was praktisch auf eine teilweise Erstattung der von den Gesellschaften gezahlten Körperschaftsteuer hinausläuft.

Auch in Frankreich stellt die Steuergutschrift nur bei Dividenden französischer Gesellschaften eine Rückerstattung eines Teils der Körperschaftsteuer zugunsten des Aktionärs dar; denn bei Dividenden ausländischer Gesellschaften ist die Steuergutschrift – trotz des äußeren Anscheins – lediglich die Rückerstattung eines in Frankreich oder im Land des Sitzes der Gesellschaft (im Falle des Bestehens eines Abkommens zwischen Frankreich und diesem letzteren Land) vorgenommenen besonderen Abzugs. Der französische Aktionär, der eine Dividende von 100 versteuert, ist berechtigt, weitere 50 auf seine Einkommensteuer anzurechenen oder die

vollständige oder teilweise Rückerstattung dieser Summe zu verlangen, falls er sonst keine Steuer zu zahlen hat. Handelt es sich um Dividenden einer französischen Gesellschaft, so hat die Dividende von 100 keinerlei Quellenabzug unterlegen: Die angerechneten 50 sind somit die Rückerstattung einer zu Lasten der Gesellschaft vor Ausschüttung der Dividende gezahlten Steuer. Im Falle einer ausländischen Dividende von 100 wird ein Abzug von 33,3% vorgenommen, und allein dieser Abzug kann angerechnet werden. Die effektiven Einkünfte des Aktionärs betragen also nur 100 gegenüber 150 bei einer französischen Gesellschaft, die eine gleich hohe Dividende ausschüttet. Die Auswirkungen dieses Systems sind folglich, je nachdem, ob es sich um eine französische oder um eine ausländische Gesellschaft handelt, grundverschieden.

21. Soweit alle gegenwärtigen Aktionäre die Steuergutschrift in Anspruch nehmen können, wird der Gesellschaft mit einem solchen Verfahren eine Reihe von Möglichkeiten eröffnet, die von der Erhaltung des Nettoertrags für den Aktionär (durch Senkung der Dividende bis zur Höhe der Steuergutschrift und entsprechende Erhöhung der Selbstfinanzierung) (1) bis zur Erhaltung der Dividende (mit entsprechender Erhöhung des Nettoertrags für die Aktionäre) mit dem Ziele reicht, durch Verminderung der innerstaatlichen Doppelbesteuerung, d.h. der Häufung der Körperschaftsteuer und der Einkommensteuer, die Fremdfinanzierung der Unternehmen mit Beteiligungskapital zu erleichtern.

22. Bei den Aktionären kann die Einführung der Steuergutschrift unterschiedliche Folgen haben. So könnten sich infolge der gestiegenen Ertragsmöglichkeiten an der Börse Kursgewinne ergeben. Ferner ist es wahrscheinlich, daß die Aktien des Landes der Steuergutschrift für Gebietsansässige interessanter sind als für Gebietsfremde und daß außerdem die Gebietsansässigen den Aktien ihres eigenen Landes gegenüber ausländischen Aktien den Vorzug geben. Damit gerät aber die "Steuergutschrift" in ihrer heutigen Gestalt in unmittelbaren Gegensatz zu dem Grundsatz, daß die Besteuerung die Wahl des Anlageortes nicht beeinflussen soll.

23. Ganz abgesehen davon, daß man den Erfolg einer so umständlichen Maßnahme bei den Aktionären bezweifeln kann, gibt die Steuergutschrift in ihrer heutigen Form im wesentlichen wegen der unterschiedlichen Behandlung von inländischen und ausländischen Dividenden sowie von Gebietsansässigen und Gebietsfremden zu erheblichen Bedenken Anlaß.
Um diese besondere Behinderung des Kapitalverkehrs zu vermeiden wäre es denkbar, dieselbe Steuergutschrift auch bei Dividendenzahlungen ausländischer Gesellschaften zu gewähren. Eine marktkonformere Lösung bestünde darin, daß die Gebietsfremden eine der Steuergutschrift entsprechende Rückvergütung der Körperschaftsteuer erhalten. Der ausgeschüttete Gewinn würde – wie es in Deutschland bereits der Fall ist – mit einem niedrigeren Körperschaftsteuersatz belastet werden. Die Zielsetzung bliebe dabei dieselbe wie bei der Steuergutschrift; man würde jedoch die mit ihr verbundenen diskriminierenden Wirkungen vermeiden.

24. Sollte sich das Prinzip einer geringeren Besteuerung des ausgeschütteten Gewinns allgemein durchsetzen, dann wäre es wün-

(1) Dies ist keine rein theoretische Annahme, denn seit Inkrafttreten des französischen Gesetzes konnten bereits zahlreiche Fälle dieser Art beobachtet werden.

schenswert, daß dieser niedrigere Steuersatz in allen Staaten die gleiche Höhe hat; bei der Förderung einer relativen Entwicklung der einzelnen Anlage- und Finanzierungsarten bietet nämlich eine einheitliche Besteuerung in den einzelnen Ländern die größte Gewähr für ein reibungsloses Funktionieren des Kapitalmarktes.

B. ANLEIHENBESITZ NATÜRLICHER PERSONEN

25. Durch die Unterschiede in der steuerlichen Behandlung der Zinserträge werden die Rentenmärkte noch stärker voneinander isoliert als die Aktienmärkte. Beim Erwerb einer Aktie kann die Erwartung eines Kursgewinns der wichtigste Beweggrund sein, während die Dividendenerwartung nur nebensächlich ist; beim Kauf einer Obligation spielt die Rendite immer eine wesentliche Rolle.
Die steuertechnischen Hindernisse zwischen den Rentenmärkten entsprechen denen zwischen den Aktienmärkten.

26. Der Anleihenbesitz von Personen, die ihre Anleihenerträge bei der Steuererklärung angeben, kann eine unterschiedliche Rendite ergeben; dies hängt davon ab, ob sie ihren Wohnsitz im Emissionsland oder im Ausland haben, ob ein Quellensteuerabzug im Ausland stattfindet und ob dieser Steuerabzug im Wohnsitzland des Anleihebesitzers nicht rückvergütet wird oder voll anrechenbar ist. Einige Länder geben allen bei ihnen aufgelegten Anleihen dadurch ein internationales Gepräge, daß sie keinen Quellenabzug vornehmen. Andere Staaten, die sich nicht nach diesem Grundsatz richten, haben jedoch bei bestimmten Anleihen der öffentlichen Hand oder ihr unterstehender Einrichtungen auf den Quellensteuerabzug verzichtet. Diese unterschiedliche Behandlung einzelner Anleihearten dürfte außer in Italien im Verschwinden sein; dort besteht ein besonderes System. Auf die Zinsen italienischer Obligationen wird eine besondere Steuer („imposta di ricchezza mobile", Klasse A) mit 32% erhoben, die es in keinem anderen Mitgliedstaat gibt. Diese (theoretisch zu Lasten des Anleihegläubigers gehende, jedoch vom Anleiheschuldner einbehaltene und abgeführte) Steuer ist eine Zedularsteuer (Steuer für eine bestimmte Einkommensart) und kann deshalb in keinem Falle auf die Steuerschuld des Anleihegläubigers für sein Gesamteinkommen angerechnet werden. Dadurch wird die Obligation in Italien für Privatunternehmen zu einem verhältnismäßig teureren Finanzierungsinstrument.
Das reibungslose Funktionieren eines internationalen Kapitalmarktes erfordert für Anleihen- wie für Aktienerträge, daß ausländischen Inhabern die Quellensteuerabzüge erstattet oder auf die Steuerschuld im Wohnsitzland angerechnet werden. Die möglichen Verfahren wurden im Abschnitt über die Aktien behandelt, da sich für den Anleihenmarkt ein anderes Hauptproblem stellt.

27. Die wichtigsten Probleme für die Rentenmärkte stellen sich auf einem anderen Gebiet. Von Land zu Land, manchmal sogar von Anleihe zu Anleihe, bestehen beträchtliche Unterschiede in der steuerlichen Behandlung der Zinsausschüttungen an Gebietsfremde, die unter kein Doppelbesteuerungsabkommen fallen, sowie an Personen, welche ihre Anonymität wahren. Diese unterschiedliche Besteuerung kann zur Folge haben, daß auch die Finanzierungskosten bei Anleihenauflegung in den einzelnen Ländern voneinander abweichen. Wenn nämlich die Kapitalmärkte integriert werden, muß dem Anleihekäufer zwangsläufig in allen Ländern die gleiche Nettorendite geboten werden.

Werden demnach die Zinsen einiger Anleihen einem Quellensteuerabzug unterworfen, dann muß ihn der Anleiheschuldner praktisch durch eine höhere Bruttoverzinsung übernehmen, soweit der Anleihegläubiger diesen Steuerabzug als endgültige Steuer und nicht als Vorauszahlung auf einer Steuer betrachtet, die er ohnehin zu zahlen hätte (d.h., falls der Anleihebesitzer den Abzug nicht anrechnen kann oder die Einkünfte der Steuerverwaltung seines Wohnsitzlandes nicht erklärt). Daher können die Finanzierungskosten bei einer Anleihe, von deren Zinsen ein Quellensteuerabzug vorgenommen wird, niemals niedriger sein als ohne Steuerabzug; sie können aber dann um den Betrag des Steuerabzugs höher sein, wenn Anleger, die ihre Zinseinnahmen versteuern und den Steuerabzug anrechnen können bzw. ihn erstattet bekommen, sich nur in einem beschränkten Umfang für eine bestimmte Anleihe interessieren.

28. Soweit die unterschiedliche Besteuerung der Anleihen in den einzelnen Ländern zu unterschiedlichen Kosten für diese Finanzierungsart führt, können sie auch bei den übrigen Finanzierungsarten unterschiedliche relative Kosten zur Folge haben. Die Arbeitsgruppe sieht in solchen Kostenunterschieden, wie bereits dargelegt wurde, ein Haupthindernis für das reibungslose Funktionieren eines europäischen Kapitalmarktes, zumal es sich um Kostenunterschiede handelt, deren Ausmaß sich ständig ändern kann.

29. In allen Mitgliedstaaten müßten anonyme Anleihegläubiger einheitlich behandelt werden. Theoretisch gibt es dafür zwei Möglichkeiten: Verzicht auf jeden Steuerabzug oder Anwendung des gleichen Steuersatzes in allen Ländern.
Im zweiten Falle könnte ein relativ niedriger Steuersatz angebracht sein. Es ist nämlich festzustellen, daß sich der Rentenmarkt in denjenigen Ländern stärker entwickelt hat, in denen die Einkünfte aus festverzinslichen Wertpapieren de jure oder de facto keiner Besteuerung unterliegen.
Während sich die Aktiengesellschaften bei den von ihnen ausgeschütteten Dividenden einem Quellensteuerabzug in dem Sitzlande nicht entziehen können, es sei denn durch eine Sitzverlegung, können Gesellschaften, die eine Anleihe auflegen wollen, ohnehin dem Steuerabzug entgehen, indem sie die Anleihe in einem solchen Lande auflegen, das keinen Quellenabzug vornimmt.

30. Die Besteuerung der Anleihen wirft auch noch ein anderes Problem auf. Es gibt nämlich auch bei den Anleihen einige Vorteile, die nur Gebietsansässigen zugute kommen.
In Belgien beispielsweise wird den Gläubigern bestimmter Staatsanleihen eine „Steuergutschrift" zum normalen Satz gewährt, obwohl kein Quellensteuerabzug vorgenommen wurde, da die Anleihen auf Grund eines Vorrechtes, das zu einer Zeit gewährt wurde, als ein inzwischen geändertes Steuersystem herrschte, steuerfrei sind. Die praktische Bedeutung dieser Steuergutschriften ist gering, sofern die Anleiheinhaber anonym bleiben wollen.
Deutschland, das von den Zinsen bestimmter Anleihearten zunächst keinen Quellensteuerabzug vornahm, auch wenn sie Anleihegläubigern zuflossen, die dem Fiskus „anonym" blieben, führte dann einen auf gebietsfremde Anleihebesitzer beschränkten Steuerabzug von 25% ein; dies läuft vor allem auf eine tatsächliche Diskriminierung zwischen solchen gebietsansässigen und gebietsfremden Gläubigern hinaus, die dem Fiskus die Einkünfte aus diesen Schuldverschreibungen nicht erklären, denn wenn sie die Einkünfte aus deutschen Anleihen im

Lande ihres Wohnsitzes erklären, wird in zahlreichen Fällen Ausländern der Steuerabzug zumindest teilweise erstattet oder angerechnet. Die Einführung dieses Steuerabzugs führte zu umfangreichen Verkäufen durch ausländische Anleiheinhaber, die anonym bleiben wollten oder weder die Erstattung noch die Anrechnung des Steuerabzugs erreichen konnten, weil zwischen ihrem Land und Deutschland kein Doppelbesteuerungsabkommen besteht oder die einseitige Anrechnung von im Ausland erhobenen Steuern nach den Rechtsvorschriften ihres Landes nicht möglich ist.

31. Bei dem Übergang von den heutigen zu den angestrebten Verhältnissen auf den Rentenmärkten stellt sich ein echtes Problem. Mit der Änderung der Besteuerung einer Anleihe kann sich für bestimmte Personenkreise die Rendite ändern, und dies kann zu einer Kursänderung führen. Daher wäre es nach Ansicht der Sachverständigengruppe besser, nicht für alle umlaufenden Anleihen mit unterschiedlichem Steuerstatus von vornherein ein gemeinsames Verfahren anzuwenden, sondern den Übergang dadurch zu erleichtern, daß eine eventuelle Gemeinschaftsregelung nur für neu ausgegebene Anleihen gelten würde, außer wenn die neue Regelung günstiger ist als die bisherigen, in welchem Falle man die alten Anleihen den neuen gleichstellen könnte. Für das reibungslose Funktionieren des Kapitalmarktes erscheint es ihr nämlich vordringlich, das Vertrauen der Kapitalanleger zu erhalten, die damit rechneten, daß die im Zeitpunkt der Emission geltende Besteuerung während der gesamten Dauer einer Anleihe wenigstens nicht schlechter wird.

IV. ÄNDERUNG DER DIREKTEN BESTEUERUNG BEI KAPITALANLAGEN DURCH FINANZINSTITUTE

32. Die Besteuerung der Einkünfte aus Kapitalanlagen von Finanzinstituten wirft, von der Entwicklung und dem reibungslosen Funktionieren eines europäischen Kapitalmarktes her gesehen zweierlei Probleme auf. Zunächst muß vermieden werden, daß die Besteuerung die Wahl des Landes beeinflussen kann, in dem diese juristischen Personen ihr Kapital anlegen.
Sodann müssen natürliche Personen, statt ihre Kapitalanlagen selbst vorzunehmen, sie bestimmten Finanzinstituten übertragen können, ohne daß ihnen dies steuerliche Nachteile bringt.

A. KAPITALANLAGEN DER INSTITUTIONELLEN ANLEGER

33. Wenn vermieden werden soll, daß die Finanzinstitute für ihre Anlagen aus steuerlichen Gründen bestimmte Länder bevorzugen, genügt es, soweit die Finanzinstitute diese Kapitalanlagen als institutionelle Anleger selbst und nicht nur als Vermittler vornehmen, wenn die vom Quellenland nicht erstatteten Auslandsabzüge in dem Land voll angerechnet werden können, in dem die Finanzinstitute (mit eventueller Rückerstattung einer Überzahlung) besteuert werden, und es keine Sondervergünstigungen gibt, die auf Kapitalanlagen in diesem Lande beschränkt sind.
Das Problem der Erstattung oder der Anrechnung von Auslandssteuerabzügen besteht bei institutionellen Anlegern (Versicherungsgesellschaften und Pensionskassen) genauso wie bei natürlichen Personen und erfordert generell die gleichen Lösungen. Bei den Finanzinstituten, die dem Ausland Direktkredite einräumen, ist ferner zu berück-

sichtigen, daß die bisherigen Lösungen mehrerer Mitgliedstaaten eine gewisse Übereinstimmung mit den in Ziffer 27 über Wertpapieranlagen untersuchten Lösungen aufweisen. Die Besteuerung der Zinsen aus Direktkrediten kann nämlich zur Doppelbesteuerung führen, falls der Schuldner in Frankreich, Belgien und Italien ansässig ist, da in diesen Ländern ein Quellenabzug auf diese Zinsen, wie auf Zinsen aus Obligationen erhoben wird. In den Niederlanden dagegen wird überhaupt kein Steuerabzug auf Zinseinkommen erhoben; dasselbe gilt in Deutschland und in Luxemburg für Zinseinkommen, die nicht aus Anleihebesitz herrühren.

34. Eine zusätzliche Schwierigkeit ergibt sich jedoch aus einer Besonderheit der Besteuerung der Einkünfte juristischer Personen in einigen Mitgliedstaaten. Die im Wohnsitzland von den Einkünften einer natürlichen Person abgezogenen Steuern sind ganz allgemein nicht nur auf die Steuerschuld dieses Steuerpflichtigen anrechenbar, sondern auch erstattungsfähig, wenn sie die Steuerschuld übersteigen. Zwar wenden einige Länder dieses Verfahren auch auf die Einkünfte juristischer Personen an, doch sehen andere nur die Anrechnung, nicht aber die Erstattung vor. Der Steuerabzug könnte also unter bestimmten Voraussetzungen eine endgültige Steuer darstellen.
Praktisch ist nicht zu beurteilen, welchen Einfluß diese endgültige Steuer gegenwärtig auf die Entscheidungen institutioneller Anleger ausübt, weil gleichzeitig noch andere Unterschiede in der Besteuerung bestehen – besonders in bezug auf die Anrechnungsmöglichkeit von ausländischen Quellensteuerabzügen – die sich ebenfalls auf die Anlagenstruktur auswirken können.

B. KAPITALANLAGEN VON BETEILIGUNGSGESELLSCHAFTEN, INVESTMENTGESELLSCHAFTEN, INVESTMENTFONDS ODER ÄHNLICHEN INSTITUTEN

35. Bei Kapitalanlagen durch Finanzinstitute, die ihre Erträge normalerweise an natürliche Personen oder andere juristische Personen weiterleiten, sollte ein zusätzlicher Grundsatz angewendet werden, der die Entwicklung und das reibungslose Funktionieren eines europäischen Kapitalmarktes begünstigen würde. Hier sind Verfahren angebracht, welche die Gewähr für eine neutrale Besteuerung bieten, d.h. Lösungen, bei denen die an andere Personen weitergeleiteten Einkünfte aus Anlagen ihnen zufließen, als ob sie diese Anlagen unmittelbar vorgenommen hätten; denn Personen, die ihre Ersparnisse von Finanzinstituten verwalten lassen wollen, die dafür besonders geeignet sind, sollten nicht durch eine zusätzliche Besteuerung bestraft werden. Dies setzt voraus, daß bei diesen Lösungen keine zusätzliche Steuer auf die Erträge aus den betreffenden Kapitalanlagen beim Finanzinstitut erhoben werden und daß außerdem der letzte Einkommensbezieher die Quellensteuerabzüge anrechnen kann, die dem Finanzinstitut noch nicht erstattet oder angerechnet worden sind.
Die Verwaltung von Sparkapital durch Finanzinstitute kann sehr unterschiedliche Formen annehmen. Den Extremfall bilden solche Institute, die kaum noch als reine Vermittler zu betrachten sind, weil sie die Verwaltung von Beteiligungen zum Ziele haben, die ihnen eine wirkliche Kontrolle über bestimmte Unternehmen verschaffen. Es erscheint wünschenswert, sie ebenfalls zu behandeln, weil sich auch bei ihnen das Problem der Steuerneutralität ergibt. Es liegt jedoch nicht in der Absicht der Sachverständigengruppe, an dieser Stelle trotz der gleichen

Steuerprobleme die Frage des Verhältnisses zwischen Mutter- und Tochtergesellschaften zu untersuchen; da es sich in diesem Fall weniger um Kapitalanlagen, sondern vielmehr um die Verwaltung von Beteiligungen handelt, würde der Rahmen dieser Untersuchung überschritten werden.

36. In den Ländern der Gemeinschaft werden die über Aktiengesellschaften üblicher Art laufenden Kapitalerträge zweimal besteuert, weil sie zusätzlich zum Quellenabzug auch noch der Körperschaftsteuer unterliegen. Von diesem Grundsatz sind nur die Dividenden ausgenommen, die belgischen Gesellschaften zufließen: Die Körperschaftsteuer wird dort nur in Höhe von 15% (10% ab 1967) der Nettodividende erhoben; für industrielle Unternehmen gilt ein ermäßigter Steuersatz von 5%. Die Körperschaftsteuerbelastung beim Finanzinstitut ist demnach in diesem Falle gering. Für Dividenden belgischen Ursprungs gibt es keine weitere Häufung direkter Steuern, die Gesellschaft ist bei der Wiederausschüttung der Dividende quellensteuerfrei, und der Aktionär kann die bei der Erstausschüttung abgezogene Steuer anrechnen. Die Regelung für die von einer belgischen Gesellschaft wieder ausgeschütteten Dividenden ausländischer Gesellschaften ist ähnlich, aber ungünstiger, weil es in der Regel weder eine Anrechnung noch eine Erstattung des Auslandssteuerabzuges gibt. Diese Nichtanrechnung wird jedoch bei natürlichen Personen, die Aktionäre der Beteiligungsgesellschaft sind und die ihnen zufließenden Dividenden versteuern, durch die Steuergutschrift ausgeglichen, die auch für die Wiederausschüttung ausländischer Dividenden durch die belgische Gesellschaft gilt. Zudem beträgt der normale Kapitalertragsteuersatz für Auslandsdividenden bei ihrem Eingang in Belgien, sofern kein internationales Abkommen besteht, nur 10% für Einkünfte, die belgischen Kapitalgesellschaften oder ihnen gleichgestellten juristischen Personen ab 1. Januar 1965 gezahlt wurden oder zugeflossen sind.
Dieses Verfahren führt dazu, daß die belgischen Beteiligungsgesellschaften ihren Aktionären nahezu den gleichen Ertrag bieten können, der zu erzielen wäre, wenn sie diese Anlagen direkt vornähmen. Dagegen ist bei Anleihen nur die Direktanlage interessant, weil keine Steuerneutralität besteht.

37. In Luxemburg gibt es eine besondere Besteuerung für Beteiligungsgesellschaften mit dem Status einer Holdingsggeselschaft. Als solche wird dort jede luxemburgische Gesellschaft angesehen, deren ausschließlicher Gesellschaftszweck die Beteiligung aller Art an anderen luxemburgischen oder ausländischen Unternehmen und die Verwaltung sowie die Verwertung dieser Beteiligungen ist, ohne jedoch weder einen eigenen Gewerbebetrieb noch ein dem Publikum offenstehendes Handelsunternehmen zu besitzen.
Diese Holdinggesellschaften sind von den direkten Steuern befreit, die normalerweise von den Gesellschaften erhoben werden; sie unterliegen nur einigen Sondersteuern, deren Belastung gering ist. Sie sind ebenfalls vom Quellensteuerabzug von den ausgeschütteten Dividenden befreit. Dagegen wird an den Dividenden, die ihnen von luxemburgischen Gesellschaften zufließen, der Steuerabzug vorgenommen, ohne daß er erstattet oder angerechnet werden könnte. Ebenso kommen die den Holdinggesellschaften zufließenden ausländischen Kapitalerträge nicht in den Genuß eventuell in Doppelbesteuerungsabkommen vorgesehener Steuererleichterungen, da diese für Holdinggesellschaften nicht gelten. Die nicht ausgeschütteten Gewinne der Holdinggesellschaften sind praktisch steuerfrei. Gerade dieser Vorteil macht das System so attraktiv, denn damit werden Tochterge-

sellschaften mit dem Status luxemburgischer Holdinggesellschaften zu einer oft vorteilhafteren Verwaltungsform als die Direktverwaltung bestimmter Vermögensteile von Gesellschaften, die die Erträge aus diesem Vermögen reinvestieren wollen. Natürlichen Personen verschaffen die Anteile an luxemburgischen Holdings praktisch dieselben Nettoeinkünfte wie Direktanlagen unter Wahrung der Anonymität.

38. In den Niederlanden besteht für die Investmentgesellschaften, deren Gesellschaftszweck ausschließlich der Erwerb, der Besitz, die Verwaltung und die Veräußerung von Aktien ist (Beleggingsmaatschappij), eine besondere Steuerregelung. Handelt es sich um eine „Beleggingsmaatschappij", deren Aktien an der Amsterdamer oder Rotterdamer Börse gehandelt werden, so fallen die Dividenden nicht unter den steuerbaren Gewinn, soweit sie von Gesellschaften zufließen, die einer ähnlichen Steuer wie der niederländischen Körperschaftsteuer unterliegen, wodurch vor allem die luxemburgischen Holdinggesellschaften ausgeschlossen werden. Diese Steuerfreiheit gilt demnach nicht für die Zinsen normaler Anleihen. „Beleggingsmaatschappijen", deren Aktien nicht an den genannten Börsen gehandelt werden, genießen dieselbe Steuerfreiheit, wenn sie mindestens 60% der ihnen im Rechnungsjahr zufließenden Dividenden und Gewinne an ihre Aktionäre ausschütten.
Von den ausgeschütteten Dividenden dieser Investmentgesellschaften wird die normale Quellensteuer von 25% abgezogen. Bei der Wiederausschüttung von Dividenden niederländischer Gesellschaften stellt dies jedoch keine neue Belastung dar, weil die Gesellschaft den vorherigen Quellensteuerabzug anrechnen kann.
Bei der Wiederausschüttung von Dividenden ausländischer Gesellschaften hat dies eine Doppelbesteuerung zur Folge, wenn diese nicht aus Ländern stammt, die mit den Niederlanden ein Abkommen über die Erstattung oder Anrechnung des Steuerabzugs zugunsten des niederländischen Aktionärs abgeschlossen haben.
Diese Regelungen führen praktisch dazu, daß die niederländischen Investmentgesellschaften ihren niederländischen Aktionären einen ebenso hohen Ertrag verschaffen, wie sie ihn erhalten würden, wenn sie die gleichen Anlagen direkt vornähmen und die daraus zufließenden Erträge versteuerten, ausgenommen jedoch Anleihen, die besser direkt erworben werden, um eine Häufung der Körperschaftsteuer bei der Investmentgesellschaft zu vermeiden.
Die niederländischen Investmentgesellschaften können die gleiche Steuerneutralität auch ihren ausländischen Aktionären bieten, unter der Bedingung, daß diese ihren Wohnsitz in einem Lande haben, das mit den Niederlanden ein Abkommen über die Erstattung oder Anrechnung der niederländischen Steuerabzüge abgeschlossen hat.

39. Die steuerliche Behandlung der französischen Investmentgesellschaften ist insofern großzügiger als die niederländischer Gesellschaften, als sich die Körperschaftsteuerfreiheit auf Erträge aus Anleihen erstreckt (die Körperschaftsteuerfreiheit kann jedoch, wie es bei den Investmentgesellschaften mit variablem Kapital (SICAV) der Fall ist, an bestimmte Bedingungen hinsichtlich der Wiederausschüttung geknüpft sein).
Die Dividenden französischer Investmentgesellschaften sind quellensteuerfrei; die französischen Aktionäre können zudem die Vorsteuerabzüge der Investmentgesellschaften anrechnen und gegebenenfalls eine Steuergutschrift unter denselben Bedingungen wie bei einer Direktanlage erhalten.

Das Verfahren, die Dividenden von Investmentgesellschaften ausdrücklich von der Quellensteuer zu befreien, ist für ausländische Aktionäre wenig vorteilhaft, die ihre Kapitalerträge versteuern, weil in den bestehenden Abkommen die Berücksichtigung der Vorsteuerabzüge der Investmentgesellschaften bei den ausländischen Aktionären nicht vorgesehen ist.

40. In Italien gibt es nur eine „geschlossene" Investmentgesellschaft. Die ihr zufließenden Dividenden unterliegen bei ihr nicht mehr der Steuer auf Arbeits- und Kapitaleinkommen (imposta sui redditi di richezza mobile). Sie unterliegen aber in der Regel der Körperschaftsteuer (steuerfrei sind sie nur dann, wenn die zugeflossenen Dividenden dem als endgültige Steuer geltenden Abzug von 30%, nicht aber dem von 5% unterlagen). Die Investmentgesellschaft erhält eine 25%-ige Ermäßigung der Körperschaftsteuer, die allen Finanzgesellschaften eingeräumt wird, wenn 60% ihres Vermögens aus Beteiligungen an Kapitalgesellschaften bestehen (ist der Staat Aktionär der Finanzgesellschaft, dann beträgt diese Ermäßigung 40%). Die Gewinde aus der Veräußerung von Wertpapieren nun selbst die nicht ausgeschütteten Gewinne unterliegen der proportionalen Steuer auf Kapitaleinkünfte. Die ausgeschütteten Gewinne dieser Gesellschaft unterliegen bei natürlichen Personen der progressiven Zusatzsteuer zum normalen Satz. Ferner gilt das normale Quellenabzugsverfahren auch für ausgeschüttete Erträge der Investmentgesellschaft.
Die Doppelbesteuerung, die sich in der Praxis aus diesem Verfahren ergibt, ist sicher der Hauptgrund dafür, daß sich die Investmentgesellschaften in Italien nicht entwickeln konnten.

41. Der Wertpapierbestand von Investmentgesellschaften, deren Besteuerung eben beschrieben wurde, ist rechtlich Eigentum der Gesellschaften. In der Form der Anlagefonds, die es in Deutschland, Belgien, den Niederlanden und in Luxemburg gibt, gehört der Wertpapierbestand nicht der juristischen Person, die ihn verwaltet, sondern ist das Gesamthandseigentum der Anteilinhaber, die durch einen Vertrag besonderer Art mit der Verwaltungsgesellschaft verbunden sind. Die Wertpapiererträge werden niemals Eigentum des Vermögensverwalters und sind daher bei ihm nicht körperschaftsteuerpflichtig. Auch aus diesem Grunde ist die Verteilung der Wertpapiererträge beim Anlagefonds quellensteuerfrei. In- und ausländische Quellensteuerabzüge von den Einkünften, die dem Anlagefonds zufließen, sind für Anteilinhaber mit Wohnsitz im Lande des Anlagefonds bei Vorlage eines Anlageverzeichnisses erstattungsfähig oder anrechenbar wie Anlagen, die unmittelbar von den Anteilinhabers vorgenommen worden sind.
Natürliche Personen mit Wohnsitz in Belgien, die an einem belgischen Anlagefonds beteiligt sind, können unter der gleichen Voraussetzung eine Steuergutschrift für Dividenden belgischer Gesellschaften, die einem Investmentfonds zugeflossen sind, beanspruchen.
Die von den Dividenden deutscher Gesellschaften einbehaltene Quellensteuer wird den deutschen Investmentfonds erstattet. Ein solches Vorrecht ist in keinem anderen Mitgliedstaat der EWG anzutreffen; damit werden diese Fonds zu einer besonders vorteilhaften Anlageart für Personen, die den Steuerbehörden gegenüber anonym bleiben wollen.
Durch diese Behandlung werden die Investmentfonds für Personen aus dem Land des Fonds zu einer steuerlich mindestens so vorteilhaften Lösung wie Direktanlagen im

Sitzland des Fonds wie auch im Ausland.
Für Personen, die ihren Wohnsitz nicht im Sitzland des Fonds haben, ist er zumindest bei Anlagen im Lande des Fonds eine steuerlich den Direktanlagen gleichwertige Anlageform, wenn diese Personen das daraus bezogene Einkommen in ihrem Wohnsitzlande nicht versteuern. Wenn sie dieses Einkommen versteuern, wird der Fonds zu einer steuerlich ungünstigen Anlageform, weil nach den bestehenden Abkommen eine Anrechnung der Steuerabzüge von den ausgeschütteten Erträgen ausländischer Anlagefonds nicht möglich ist; nur die Steuerverwaltung im Sitzlande des Fonds erkennt die Anrechnung dieser Steuerabzüge an Hand von Anlageverzeichnissen des Fonds an.

42. Nach dieser kurzen Untersuchung der Anlagemöglichkeiten durch die Einschaltung von Finanzinstituten ist festzustellen, daß die Steuerneutralität nur in verhältnismäßig wenigen Fällen gewährleistet ist.
Bei Anlegern, die ihre Wertpapiererträge versteuern, besteht diese Transparenz für Aktien- und Anleihenerträge im Wohnsitzland wie im Ausland nur in Frankreich, Deutschland, Belgien und Luxemburg; außerdem ist die Neutralität bei den in diesen Ländern bestehenden Anlageformen in der Regel nur für Gebietsansässige verwirklicht.
In den Niederlanden ist die Neutralität nur bei Aktienanlagen vorhanden, doch kommt sie durch Abkommen auch bestimmten Ausländern zugute.

43. Damit Kapitalanlagen über Finanzinstitute in der Entwicklung des europäischen Kapitalmarktes die ihnen zukommende Rolle spielen können, müßten in den Ländern, in denen sich die bestehenden Systeme nur für einige Anlagearten eignen, die der Steuerneutralität entgegenstehenden Hindernisse auch für die übrigen Anlagearten beseitigt werden. Außerdem müßten Investmentfonds und Investmentgesellschaften in allen Mitgliedstaaten Gebietsansässigen und Gebietsfremden aus der Gemeinschaft unter den gleichen Bedingungen zugänglich sein.

44. Es ist kaum möglich, heute schon steuertechnische Lösungen vorzuschlagen, mit denen diese Ziele erreicht werden können. Die Lösungsmöglichkeiten richten sich nach den Grundsatzentscheidungen der Mitgliedstaaten über die Besteuerung der Erträge von Kapitalanlagen im Ausland vor allem nach der Entscheidung, ob man die Besteuerung in einem einzigen Land durchführt oder die Steuereinnahmen zwischen dem Quellenland und dem Wohnsitzland teilt. Zudem können diese Lösungen für Kapitalanlagen, die in dritten Ländern vorgenommen werden, unvollkommen bleiben, solange zwischen den Mitgliedstaaten und diesen Ländern Abkommen bestehen, die von unterschiedlichen Grundsätzen ausgehen.
Es dürfte wohl kaum möglich sein, diese Schwierigkeiten auf dem Gebiet der Investmentfonds und Investmentgesellschaften ohne ein multilaterales Abkommen zur Vermeidung der Doppelbesteuerung in einer Weise zu lösen, die voll befriedigt.

V. ÄNDERUNG DER INDIREKTEN BESTEUERUNG DER KAPITALAUFNAHME UND DES KAPITALVERKEHRS

45. Bei den indirekten Steuern untersuchte die Arbeitsgruppe vor allem die beiden Steuergruppen, die heute das Kapitalmarktgeschehen unmittelbarer beeinflussen, nämlich:
- die indirekten Steuern auf die Kapitalaufnahme; zu dieser Gruppe gehören vor

allem die Gesellschaftsteuer und die Wertpapiersteuer für die Aufnahme von Anleihekapital durch inländische Kapitalnachfrager sowie die indirekten Steuern bei der Börseneinführung ausländischer Wertpapiere;
- die indirekten Steuern auf die Übertragung von Wertpapieren; zu dieser Gruppe gehören die Börsenumsatzsteuer und die ihr gleichgestellten Steuern.

46. Die Gesellschaftsteuer wird vor allem bei der Gründung oder der Erneuerung (prorogation) einer Gesellschaft (oder einer ihr gleichgestellten juristischen Person), bei der Änderung der Gesellschaftsform oder des Gesellschaftskapitals erhoben. Sie ist in der Regel eine Eintragungsgebühr, außer in Deutschland, wo die Gesellschaftsteuer eine besondere Steuer ist; diese Steuern sind immer von der Gesellschaft zu zahlen, der das Kapital zufließt.

Die Wertpapiersteuer wird bei der Ausgabe von Wertpapieren im Ausgabeland oder bei dem Inverkehrbringen ausländischer Wertpapiere erhoben; bei im Ausland umlaufenden Wertpapieren können diese beiden Steuertatbestände zu einer Steuerhäufung führen.

Die Dienststellen der Kommission haben in Zusammenarbeit mit den zuständigen Behörden der Mitgliedstaaten einen gegenwärtig dem Rat vorliegenden Richtlinienentwurf über die beiden indirekten Steuerarten auf die Kapitalaufnahme ausgearbeitet. Zweck dieser Richtlinie ist die Beseitigung der Ursachen der Doppelbesteuerung und, soweit eine dieser Steuern beibehalten wird, die Einführung eines einheitlichen Steuersatzes in allen Mitgliedstaaten, um Kostenunterschiede bei den einzelnen Finanzierungsarten zu vermeiden.

Die einfachste Lösung für den ganzen Fragenkomplex wäre die Abschaffung der Wertpapiersteuer und der Gesellschaftsteuer gewesen. Die Dienststellen der Kommission schlugen dies zwar vor, doch zeigte sich, daß diese Lösung kaum die Zustimmung aller Mitgliedstaaten finden könnte. Der dem Rat vorliegende Richtlinienentwurf sieht die Abschaffung der Wertpapiersteuer und das Verbot jeglicher Ersatzsteuer sowie die einheitliche Einführung einer auf 1% ermäßigten Gesellschaftsteuer vor, die sich bei Zusammenschlüssen auf 0,50% verringert; die Erhebung dieser Steuer soll so vereinheitlicht werden, daß jede Doppelbesteuerung vermieden wird (Besteuerung grundsätzlich nur im Lande des Gesellschaftssitzes).

Die Gruppe und die Dienststellen der Kommission vertreten denselben Standpunkt. Falls die Abschaffung dieser beiden Steuern – was wünschenswert wäre – nicht verwirklicht werden kann, sollte nach Ansicht der Sachverständigengruppe wenigstens die in den erwähnten Richtlinienentwürfen vorgeschlagene Lösung angenommen werden, da diese dann noch am ehesten den angestrebten Zielsetzungen entspricht.

47. Die Börsenumsatzsteuer betrifft im wesentlichen Kassa- und Termingeschäfte in Wertpapieren. In Luxemburg wird eine solche Steuer nicht erhoben. Die Struktur der Steuersätze unterscheidet sich in den übrigen Mitgliedstaaten von Land zu Land erheblich. Deutschland und die Niederlande besteuern zudem nicht nur die Geschäfte im Inland, sondern unter bestimmten Voraussetzungen auch Geschäfte im Ausland auf Rechnung von Deviseninländern, woraus sich eine Doppelbesteuerung ergeben kann.

Die Börsenumsatzsteuersätze sind verhältnismäßig niedrig, jedoch nicht unbedeutend. Die Unterschiede zwischen den Mitgliedstaaten können daher dazu führen, daß eine Transaktion eher in dem einen als in dem anderen Land erfolgt. Diese Steuern vermindern zudem das Interesse an Arbitragegeschäften und

führen zu gewissen Marktspaltungen, weil sie Kostenunterschiede für die einzelnen Formen der Kapitalaufnahme bewirken. Aus diesem Grunde schlägt die Sachverständigengruppe vor, eher die Börsenumsatzsteuer abzuschaffen, als zur Vermeidung jeder Doppelbesteuerung in allen Ländern einheitliche Steuersätze und -erhebungsbedingungen einzuführen. Sollte über die Abschaffung der Börsenumsatzsteuer keine Einigung zustande kommen, dann wären einheitliche Steuersätze dem gegenwärtigen Zustand immer noch vorzuziehen, denn dadurch würde wenigstens die Wahl des Ortes, an dem die Transaktionen abgewickelt werden, nicht durch die Börsenumsatzsteuern beeinflußt werden.

48. Die Wechselsteuer kann bei Wechseln im internationalen Verkehr ebenfalls zu Doppelbesteuerungsvorgängen führen. Diese könnten durch ähnliche Lösungen, wie sie soeben vorgeschlagen wurden, vermieden werden.

Schlußfolgerungen

49. Soll innerhalb der Gemeinschaft ein funktionsfähiger integrierter Kapitalmarkt aufgebaut werden, so ist es erforderlich, daß die Steuersysteme das Entstehen binnenmarktähnlicher Verhältnisse nicht verhindern. Diese Neutralität der Steuersysteme besagt, daß sie weder die Wahl des Ortes der Anlage oder der Transaktion noch die Wahl des Sparens zwischen einer Direktanlage und der Inanspruchnahme der Dienste eines Finanzinstitutes beeinflussen dürfen. Steuerneutralität heißt ferner, daß es zwischen den Mitgliedsländern keine bei Entwicklung bestimmter Anlagetypen oder Finanzierungsarten durch die Steuersysteme hervorgerufene Unterschiede geben darf.

Damit diese Forderungen erfüllt werden können, ist es erforderlich, daß die Steuersysteme der Mitgliedstaaten auf bestimmten Gebieten geändert werden.

(1) Die Doppelbesteuerung der Erträge von Kapitalanlagen in einem anderen Lande als dem des Wohnsitzes des Einkommensbeziehers wären zu beseitigen. Allein unter dem Gesichtspunkt der Erfordernisse eines europäischen Kapitalmarktes läßt sich dies dadurch erreichen, daß entweder der Kapitalertrag nur in einem Land besteuert oder eine Teilung der Steuereinnahmen in der Weise vorgenommen wird, daß in dem Staat der Einkommensquelle ein Abzug stattfindet und dieser dann im Staat des Wohnsitzes des Einkommensbeziehers systematisch angerechnet wird.

Eine Beseitigung der Doppelbesteuerung ist ebenfalls auf dem Gebiet der Kapitalverkehrsteuern erforderlich. Die hierfür erforderlichen Maßnahmen werden zur Zeit erörtert; dem Rat liegt ein entsprechender Richtlinienentwurf vor, der von den Dienststellen der Kommission in Zusammenarbeit mit den zuständigen Stellen der Mitgliedstaaten ausgearbeitet wurde.

(2) Abzuschaffen ist ferner die noch immer bestehende steuerliche Benachteiligung der Kapitalanlagen in anderen Mitgliedstaaten durch Vermittlung von Finanzinstituten. Die Lösungsmöglichkeiten werden davon abhängen, welche grundsätzliche Haltung die Mitgliedstaaten hinsichtlich der Besteuerung der Erträge von im Ausland vorgenommenen Kapitalanlagen einnehmen werden. Infolge der verwickelten rechtlichen Beziehungen zwischen den an derartigen Anlagen beteiligten verschiedenen Parteien kann eine Steuerneutralität wahrscheinlich in voll zufriedenstellender Weise nur im Rahmen eines multilateralen Doppelbesteuerungsabkommens gewährleistet werden, das auch

die Frage der Holdinggesellschaften und Investmentfonds ausdrücklich regelt.

(3) Es sollten keinerlei Steuervorteile gewährt werden, die auf Anlagen in bestimmten Ländern beschränkt sind: Dies erfordert eine Änderung der Systeme der „Steuergutschrift", die bewirken, daß ein Teil der Körperschaftsteuer gegenwärtig allein den Gebietsansässigen bei Dividenden inländischer Gesellschaften rückerstattet wird. Die Lösung, die dem Erfordernis eines reibungslosen Funktionierens eines europäischen Kapitalmarktes am besten gerecht würde, bestünde darin, diese Erstattung auf die Gebietsfremden auszudehnen.

(4) Zwischen den Mitgliedsländern bestehen zur Zeit noch zahlreiche Unterschiede in der steuerlichen Behandlung der Kapitalerträge von Gebietsfremden oder von Personen, welche ihre Anonymität wahren. Bei diesen Einkünften wäre eine Harmonisierung der Besteuerungs- und Kontrollsysteme erforderlich. Diese Frage ist für den Rentenmarkt von ganz besonderer Bedeutung, da Ertragserwartungen bei der Wahl von Anlagen in Rentenwerten eine ausschlaggebende Rolle spielen. Die Harmonisierung könnte darauf hinauslaufen, jeglichen Quellenabzug bei Zinsen auf Obligationen zu beseitigen oder in sämtlichen Mitgliedstaaten einen Abzug zum gleichen Satz vorzusehen.

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DEUTSCH-FRANZÖSISCHES STEUERWÖRTERBUCH (See Germany)

GERMANY

DEUTSCH-FRANZÖSISCHES STEUERWÖRTERBUCH, Volume I, compiled by Kovarik, Dr. Miroslaw. Published by Franz Nowack Verlag, Frankfurt am Main, 1964, 82 pp.
The author attempts to translate in the first part of this French-German dictionary all German tax terms into their French equivalents, with some examples where appropriate. Only German terms where special meanings have gradually been established over the years, are however dealt with. General terms, in common use, which have retained their literal meaning, are not covered.
As the tax systems in the EEC countries differ from one another, it is evident that each term to be translated must be explained in its context with its particular tax system, and the purpose for which it is provided and the statutes in which it is applied. The author is therefore of the opinion that this is the only way of translating tax terms from one language to another. The second part (French-German) will be based on the same principle.

Library International Bureau of Fiscal Documentation, no. B 272.

DIE STEUERLICHEN VORTEILE AUSLÄNDISCHER KAPITALGESELLSCHAFTEN GEGENÜBER INLÄNDISCHEN BEI DIREKTINVESTITIONEN IN DER BUNDESREPUBLIK DEUTSCHLAND UNTER BESONDERER BERÜCKSICHTIGUNG DES GESPALTETEN KÖRPERSCHAFTSTEUERSATZES, by Kraushaar, R. Published by the Centrale für GmbH Dr. Otto Schmidt, Cologne-Mariënburg, 1966.
Thesis concerning tax benefit for foreign corporations in comparison to resident corporations in case of direct investments (permanent establishment, subsidiary) in the German Federal Republic with special attention to the German corporate split rate of tax. As comparative analysis the tax treatment of corporations resident in France, the Netherlands, Switzerland, the United Kingdom and the United States are taken into consideration including the effect from tax treaties for the avoidance of double taxation. The tax burden of corporate income tax, net worth tax, business tax, sales tax and capital transactions taxes are included in the approach.

Library International Bureau of Fiscal Documentation, no. B 247.

THEORIE UND PRAXIS DES GESAMTWERTS UND GESCHÄFTSWERTES DER UNTERNEHMUNG, by Kolbe, Kurt. Published by the Verlagsbuchhandlung des Instituts der Wirtschaftsprüfer GmbH., Düsseldorf, 1967, 236 pp.
The author discusses the theoretical and practical methods employed in assessing an enterprise's goodwill value for purposes of sale. This revised third edition—the first was published under the title "Gesamt- und Geschäftswert der Unternehmung" (Cologne, 1954) and the second under the name "Ermittlung von Gesamtwert und Geschäftswert der Unternehmung" (Düsseldorf, 1959)—considers additional questions such as the affect of taxation on the goodwill value and the "amortization provisions" relating to goodwill for commercial and tax balance sheet purposes.

Library International Bureau of Fiscal Documentation, no. B 115.

DIE ERTRAGSBESTEUERUNG INLÄNDISCHER BETRIEBSTÄTTEN UND TOCHTERGESELLSCHAFTEN AUSLÄNDISCHER KAPITALGESELLSCHAFTEN – Ein Beitrag zum internationalen Steuerrecht – by Mersmann, Wolfgang. Published in the series „Steuerrecht und Steuerpolitik", Volume 5, by Verlagsgesellschaft Recht und Wirtschaft GmbH., Heidelberg, 1967, 217 pp., price DM 23,—.
Authoritative publication on the subject income taxation of German permanent establishment and subsidiaries of nonresident corporations. In this contribution to international tax law attention is paid to the allocation problem of profits. An extensive list of literature is appended.

Library International Bureau of Fiscal Documentation, no. B 108.

DIE DEUTSCHEN ZOLLVORSCHRIFTEN. Zölle und sonstige Eingangsabgaben sowie nichtaussenwirtschaftliche Einfuhrbeschränkungen. Published by the Bundesstelle für Aussenhandelsinformation, Cologne, 1966, 92 pp.
A short survey of the German customs duties regulations.

Library International Bureau of Fiscal Documentation, no. B 277.

DIE VORSTANDSPFLICHTEN BEI VERLUST, ZAHLUNGSUNFÄHIGKEIT UND ÜBERSCHULDIGUNG EINER AKTIENGESELLSCHAFT, by Hirtz, Herbert. Published by the Verlagsbuchhandlung des Instituts der Wirtschaftsprüfer GmbH., Düsseldorf, 1966, 136 pp.
The provision in the new Corporation Act regarding the action to be taken by the Executive Board of Directors in cases where a corporation incurs big losses, and is unable to pay its debts or is in a position of excessive indebtedness. The book is written from an industrial economical view point. A list of publications on this subject is appended.
Library International Bureau of Fiscal Documentation, no. B 274.

WIRTSCHAFTSPRÜFUNG IM NEUEN AKTIENRECHT, published by the Verlagsbuchhandlung des Instituts der Wirtschaftsprüfer GmbH., Düsseldorf, 1966, 166 pp.
The text of the papers delivered at the 12th conference of German accountants between September 29 and 30, 1966 in Frankfurt am Main. The subject of the conference was "Accountancy under the new Corporation Law".
Library International Bureau of Fiscal Documentation, no. B 276.

In the Forkel-series Recht und Steuern, Forkel-Verlag, Stuttgart has published GMBH & CO. Plädoyer für die moderne Unternehmensform. Wirtschaftlich, handelsrechtlich, steuerlich, by Böttcher, Conrad, G. Krahmer, J. Beinert. 1966, 143 pp.
The economic, commercial and tax aspects of the popular legal form the GmbH and Co. are extensively treated.
Libray International Bureau of Fiscal Documentation, no. B 269.

BEWERTUNGSGESETZ MIT DURCHFÜHRUNGSBESTIMMUNGEN. Kommentar, by Steinhardt, Rolf. Published by W. Kohlhammer Verlag, Stuttgart and Deutscher Gemeinder Verlag, Cologne, 1966, 4th edition (revised), 1st delivery XI 566 pp., price DM 48,— in addition DM 4,50 for the cover.
This is the fourth, completely revised edition in loose-leaf form of this work covering the Valuation Act and the regulations pertaining thereto as amended on December 10, 1965 (BGBl. I S 1862) with commentary and, where appropriate, examples provided.
Library International Bureau of Fiscal Documentation, no. B 172.

STEUERBERATER-JAHRBUCH 1966/67 zugleich Bericht über den XVIII. Fachkongress der Steuerberater der Bundesrepublik Deutschland. Published by Verlag Dr. Otto Schmidt KG., Cologne, 1967, 520 pp.
Report on the meeting held in November 1966 by the Association of Tax Advisors in Germany. Amongst those who contributed were: Prof. Dr. Gerhardt Wacke, Dr. Lüder Meyer-Arndt, Dr. Rudolf Thiel, Gerhard Thoma, Rudolf Grieger, Conrad Böttcher.
Library International Bureau of Fiscal Documentation, no. B 164.

INDIA

SALARIES AND INCOME TAX, by Lakhotia, Ram Niwas. Published by Asha Publishing House, P-16, C.I.I. Road, Calcutta, 1966, 309 pp.
This book incorporates the changes effected by all amending enactments including the Finance Act, 1966 and the allied Income Tax rules in so far as they affect directly or indirectly on different aspects of income tax levy.
Library International Bureau of Fiscal Documentation, no. B 220.

INTERNATIONAL

FISCAL HARMONIZATION IN COMMON MARKETS, by Shoup, Carl S.
Volume I: THEORY,
Volume II: PRACTICE.
Published by the Columbia University Press, New York—London, 1967, 468 and 661 pp.
The first volume, Theory, does not contain many descriptions or analyses of concrete cases. The second volume, Practice, contains—many theoretical analyses. This a-symmetry is inevitable; theory can be fruitfully discussed without practice, but not practice without theory.
Library International Bureau of Fiscal Documentation, no. B 213.

RELIEF FROM DOUBLE TAXATION, by Tempel, A.J. van den. Chapter 7 of "Developments in Taxation since World War I". Published by the International Bureau of Fiscal Documentation, Amsterdam, 1967, 54 pp.
A comparison of the work of the League of Nations and the Organisation for Economic Cooperation and Development. Available also in German.
Library International Bureau of Fiscal Documentation, no. B 237.

NETHERLANDS

DE OMZETBELASTING EN DE MIDDENSTAND, by F. Kuipers. Published by F. Kuipers – Fiscale Uitgaven en Adviezen, Nijmegen, 1964, 5th edition, loose-leaf.
This book is wholly revised. It deals with the turnover tax as it applies to each branch of trade or business.
Library International Bureau of Fiscal Documentation, no. B 212.

SPAIN

ALLGEMEINE EINKOMMENSTHEORIE, by Alba, M. Albizu. Published by Franz Nowack Verlag, Frankfurt am Main, 1964, 120 pp. price DM 16,80.
This is a German translation by Klaus Wellenreuther of a Spanish book describing the Spanish approach to income.
Library International Bureau of Fiscal Documentation, no. B 278.

SWITZERLAND

SCHWEIZERISCHES STEUER-LEXIKON, Band I: LEXIKON, Band II: BUND, KANTONE, GEMEINDEN, by Gygax, E., R. Chevalier, F. Koebel, B. Zingg. Published by Verlage Organisator, Zürich, 1967, 291 and 224 pp. resp.
The seventh edition of this quick-reference work on the federal, cantonal and municipal taxes, designed to point out the possibilities of avoiding double intercantonal taxation. The first volume is a dictionary containing explanatory notes to the practical assessment of taxes, arranged in alphabetical order of key words. Volume II contains details over the different tax laws valid in the Federation and the different cantons and municipalities.
Library International Bureau of Fiscal Documentation, no. B 238.

UNITED KINGDOM

REPORT OF THE COMMISSIONERS OF HER MAJESTY'S INLAND REVENUE FOR THE YEAR ENDED 31st MARCH 1966 – 109th Report. Published by Her Majesty's Stationery Office, Kingsway, London, 1967, 253 pp., price £1.4.—.
The principal Inland Revenue duties in force during the year under review (1965-1966) consisted of the following: income tax, surtax, profits tax, estate duty and stamp duties.
Library Interantional Bureau of Fiscal Documentation, no. B 215.

CLOSE COMPANIES, by Mustoe, N.E. Published by Butterworths, London, 1965, 283 pp.
Handbook to the taxation of "close companies" as defined under the 1965 Finance Act. The book is divided into two principal parts: the first deals with the "law special to close companies" and discusses, in separate chapters, the definition of the term "close company" and the various consequences for "close company" status for distributions, directors' remuneration, and other topics, the second provides a survey of the corporation tax and the capital gains tax, as introduced by the 1965 Finance Act. Relevant legislative extracts and an index are also included.
Library International Bureau of Fiscal Documentation, no. B 270.

CORPORATION TAX, by Hughes, P.F. and T.L.A. Graham. Published by the Taxation Publishing Company Limited, London, 1966, 884 pp., price 65 s.
Handbook to the corporation tax which was introduced by the 1965 Finance Act. Numerous computative examples are provided together with the reproduction of relevant legislation.
Library International Bureau of Fiscal Documentation, no. B 269.

SEVEN-YEAR DIGEST OF INCOME TAX CASES CLASSIFIED 1959–1965, by Skottowe, P.F. Published in continuation of "Butterworths Income Tax Digest", Butterworths, London, 1966, 190 pp.
Summaries of important income tax cases brought before English, Scottish, Irish and Commonwealth courts. By way of its classification and numbering, the book has been specially designed to supplement the Butterworths Income Tax Digest. All cases fully reproduced or simply referred to are provided for in the index.
Library International Bureau of Fiscal Documentation, no. B 268.

U.S.A.

READINGS IN THE ECONOMICS OF TAXATION, by Mushgrave, R.A. and C.S. Shoup, selected by a committee of The American Economic Association. Published by Richard D. Irwin, Inc., Homewood, Illinois, 1959, 581 pp., price US $ 7.—.
The economics of taxation appear the most appropriate topic for the present, since it represents the area of public finance in which the

major body of economic analysis has been developed.

Library International Bureau of Fiscal Documentation, no. B 233.

READINGS IN FISCAL POLICY, by Smithies, A. and J.K. Butters, selected by a committee of The American Economic Association. Published by Richard D. Irwin, Inc., Homewood, Illinois, 1955, 596 pp., price US $ 7.—.
This volume attempts not only to cover the field of fiscal policy but to show how doctrine on the subject has evolved over the past generation.

Library International Bureau of Fiscal Documentation, no. B 234.

1967 FEDERAL TAX HANDBOOK. Published by Prentice Hall, Inc., Englewood Cliffs, New Jersey, 1967.
This book is designed for those who want a quick answer in digest form to a specific tax problem, without the need for looking up the law or the more detailed text coverage in the Prentice Hall "Complete Federal Tax".

Library International Bureau of Fiscal Documentation, no. B 171.

INTERNAL REVENUE BULLETIN, CUMULATIVE BULLETIN 1966 – 1. Published by the Treasury Department, Internal Revenue Service, January – June 1966, 677 pp.
A collection of all rulings, decisions and procedures pertaining to internal revenue matters published in the weekly Internal Revenue Bulletins, Nos. 1966 -1 to 1966 -2, inclusive. It is the policy of the Service to publish in the Bulletin all substantive and procedural rulings of importance or of general interest, the publication of which is considered necessary to promote a uniform application of the tax laws.

Library International Bureau of Fiscal Documentation, no. B 169.

INTERNATIONAL TRADE, INVESTMENT AND ORGANISATION, by Weine, R, La Fave, P. Hay. Published by the University of Illinois Press, Urbana – Chicago – London, 1967, 506 pp., price US $ 7.50.
Divided into three parts, the book first explores the much debated movement to reduce tarif restrictions and U.S. taxation of foreign income. Part two is primarily focused around the present and future implications of the European Common Market. Part three considers existing problems with respect to international unification of law.

Library International Bureau of Fiscal Documentation, no. B 214.

1967 U.S. MASTER TAX GUIDE, CCH Current Law Handybook Edition. Published by Commerce Clearing House, Inc., New York – Chicago – Washington, 1966, 560 pp., price US $ 4.—.
This book is primarily designed to help tax payers in preparing their 1966 corporate and individual income tax returns. It also provides information on the tax consequences flowing from decisions and transactions which the tax payer may face in 1967.

Library International Bureau of Fiscal Documentation, no. B 170.

FOREIGN INVESTORS TAX ACT OF 1966 WITH EXPLANATION Including other Amendments to the Internal Revenue Code P.L. 89-809. As signed by the President, November 13, 1966. Published by Commercial Clearing House, Inc., 1966, 192 pp., price US $ 3.50.
This book covers the changes made in the structure of taxation of foreign corporations and individuals in the United States.

Library International Bureau of Fiscal Documentation, no. L 168.

1966 ROUNDUP OF FEDERAL TAX LAW CHANGES. Published by Commercial Clearing House, Inc., 1966, 96 pp.
A handy reference work providing clear and concise explanations to the new tax laws enacted in 1966 modifying income and gift taxation and the excise taxes.

Library International Bureau of Fiscal Documentation, no. L 186.

LOOSE-LEAF SERVICES

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DIE EINKOMMENSTEUER-RECHTSPRECHUNG, Teil III, release 5.
Wirtschaftsverlag Dr. Anton Orac, Vienna.
KOMMENTAR ZUM BEWERTUNGSGESETZ, release 7.
Wirtschaftsverlag Dr. Anton Orac, Vienna.
Steuerrechtliche Tabellensammlung:
HANDBUCH FÜR DEN STEUERPRAKTIKER, release 10.
Wirtschaftsverlag Dr. Anton Orac.

BELGIUM

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Gaston vanden Avijle, Brussels.
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C.E.D. Samson N.V., Brussels

CANADA

CANADIAN INCOME TAX, release 34.
Butterworth & Co., Toronto.
CANADA TAX SERVICE LETTER, release 102.
Richard de Boo Ltd., Toronto.
CANADA TAX SERVICES, releases 217 and 218
Richard de Boo Ltd., Toronto.
MC.DONALD'S CURRENT TAXATION, releases 6–10.
Butterworths, Toronto.
PROVINCIAL TAXATION SERVICE, release 212.
Richard de Boo Ltd., Toronto.

FRANCE

BULLETIN DE DOCUMENTATION PRATIQUE DES TAXES SUR LE CHIFFRE D'AFFAIRES ET CONTR. INDIRECTES, release 12.
Ed. Francis Lefebvre, Paris.

BULLETIN DE DOCUMENTATION PRATIQUE DES IMPOTS DIRECTS ET DES DROITS D'ENREGISTREMENT, release 13.
Ed. Francis Lefebvre, Paris.
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DROIT DES AFFAIRES, releases 3–5.
Ed. Législatives et Administratives, Paris.
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Ed. Francis Lefebvre, Paris.
Juris Classeur Fiscal:
Code Fiscal "IMPORTS DIRECTS", release 146.
Ed. Techniques, Paris.
Juris Classeur Fiscal:
Code Fiscal "CHIFFRE D'AFFAIRES", release 5146.
Ed. Techniques, Paris.
Memento Lamy:
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Services Lamy, Paris.

GERMANY

ABC FÜHRER LOHNSTEUER, release 59.
Fachverlag für Wirtschafts- und Steuerrecht, Schäfter und Co., Stuttgart.
STEUERERLASSE IN KARTEIFORM, release 66.
Dr. Otto Schmidt, Cologne.
STEUERGESETZE, release Febr.
C.H. Beck'sche Verlagsbuchhandlung, Munich.
STEUERRECHTSPRECHUNG IN KARTEIFORM, release 182.
Verlag Dr. Otto Schmidt, Cologne.

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Fiduciaire Marocaine d'Editions Techniques, Casablanca.

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D. Brouwer en Zoon, Arnhem.
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N.V. Uitgeverij FED, Amsterdam.
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b) TARIEF VAN INVOERRECHTEN, B1 releases 84 and 85.
TARIEF VAN INVOERRECHTEN, B2, release 51.
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Vermande en Zonen, Uitgevers, IJmuiden.
TERUGGAAF VAN OMZETBELASTING BIJ UITVOER, release 186.
N. Samson N.V., Alphen a/d Rijn.
VADEMECUM VOOR IN- EN UITVOER, releases 352 and 353.
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De Vakstudie-fiscale encyclopedie:
VENNOOTSCHAPSBELASTING, release 60;
OMZETBELASTING, releases 54 and 55;
REGISTRATIEWET, release 23;
WET OP DE INKOMSTENBELASTING, releases 27 and 28.
N.V. Uitg.Mij. AE.E. Kluwer, Deventer.

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NEW ZEALAND BOARD OF REVIEW DECISIONS, releases 22-24.
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SKATTE-NYTT, releases A nr 2; B nrs 4, 5, 6.
Norsk Skattebetalerforening, Oslo.

SOUTH AFRICA

LAW AND PRACTICE OF SOUTH AFRICAN INCOME TAX, releases 15.
Butterworth & Co. Ltd., Durban.

SPAIN

CIRCULARES BOLETINES DE INFORMACION, release 93.
Gabinete de Estudios (T.A.L.E.), Madrid.

TURKE

Türk Argüs Ajansi:
LA LEGISLATION TURQUE, releases 3882-3900.
Karaköy, Istanbul.

UNITED KINGDOM

BRITISH TAX ENCYCLOPEDIA, Vol. I, II, III, IV, V and VI:
releases 10 and 20.
Sweet and Maxwell Ltd., London.

U.S.A.

FEDERAL TAX GUIDE REPORTS, releases 20–24.
Commerce Clearing House, Inc., Chicago.
FEDERAL TAXES REPORT BULLETIN, releases 7–10.
Prentice Hall, Inc., New Jersey.
FEDERAL TAXES REPORT BULLETIN, release 10.
Prentice Hall, Inc., New Jersey.
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Commerce Clearing House, Inc., Chicago.
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Commerce Clearing House, Inc., Chicago.

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SUPPLEMENT TO NO 3 (Supplement B)

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EDITORIAL:

DIRECT AND INDIRECT TAXES: AN OUTDATED CLASSIFICATION

In this issue attention is paid to developments in the EEC. On page 256 the text of the first and second directive for the harmonisation of turnover taxation in the member States has been published as approved by the Council of Ministers on April 11, 1967. A brief chronological review of the most important achievements and salient events in the first ten years of the Treaty of Rome is printed on page 271 et seq. of this issue.

The terms "direct" and "indirect" taxes have been used in a number of EEC publications, such as the "Segré report", of which an abstract has been published in the previous issue of the Bulletin. We wonder whether the use of these terms could be avoided in order to achieve clarity in theoretical concepts and whether the EEC could start to avoid using these terms.

They were introduced as having a special juridical meaning during a discussion in the National Assembly in France in 1789*). Ever since that time these terms have been used, although their meaning has varied considerably. They developed in an economic sense after John Mill Stuart used them. Statisticians used these terms for their own purposes. Gradually, a considerable babel of tongues has arisen and all over the world the classification is used depending on the official's or non-official's pre-supposition of what should be considered as a direct or an indirect tax. Once a classification looses its exactitude and precision, it is worthless in an international tax discussion. It makes no sense to use terms which have specific legal meanings in some countries and which are otherwise vague, being historically infected or economically applied in different contexts as a means of classifying taxes. Would it not be better to limit the use of these terms to strictly national legal concepts, if any, and treat them only in this respect?

DR. J. C. L. HUISKAMP

*) "L'impôt direct s'entend de toute imposition assise sur les fonds de terre ou sur les personnes, qui se lève par voie du cadastre ou des rôles de cotisation, et qui passe immédiatement du contribuable cotisé au percepteur chargé d'en percevoir le produit; les contributions indirectes sont tous impôts assis sur la fabrication, la vente, le transport et l'introduction d'objets de commerce ou de consomnation."

ARTICLES

RICHARD M. BIRD*:

STAMP TAX REFORM IN COLOMBIA

Stamped paper and stamp taxes are among the oldest means of raising government revenue in most countries. In Colombia these devices date back to the colonial period and were enshrined in the first constitution of the new republic in 1821. Although stamp tax legislation has since undergone a great many changes, including quite a few since the last codification in 1960, the basic nature of the tax has not changed. Similar ancient taxes exist in countries as different as the United Kingdom, Italy, Japan, India, the United States, and apparently every country in Latin America. The revenue system of all these countries would be simpler, fairer, cheaper to administer, and no less productive if the hundreds of diverse levies which now usually constitute their stamp tax systems were drastically reformed. Such a reform is here proposed for Colombia.

I. THE COLOMBIAN STAMP TAX SYSTEM

The stamp tax as it now exists in Colombia is an irregular collection of fixed and ad valorem taxes applied to a conglomeration of bases in a confused and confusing way. These taxes may be classified for purposes of description into seventeen categories:[1]

(1) official activities (passports, various documents, papers, and certificates);
(2) mining activities (claims, titles);
(3) concessions and permits (mineral, forests, water, firearms, etc.);
(4) industrial property (patents, trademarks);
(5) transportation (ship and aircraft licenses and registration);
(6) appointments of government officials and officers of private companies;
(7) payrolls and accounts presented by government employees for payment at government offices;
(8) income tax returns (filing);
(9) external trade (consular invoices, manifests, bills of lading, etc.);
(10) notarized documents;
(11) appraisals of property;
(12) documentary evidence;
(13) transfers of money;
(14) professional and technical licenses;
(15) financial activities (issuance and transfer of bonds and shares);
(16) air and sea transportation from Colombia to foreign ports;
(17) cargo and parcel transportation (documents, parcel post).

Many of these categories can in turn be

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* Lecturer on Economics, Harvard University. Although this paper is based on some work done for the Harvard Development Advisory Service in Colombia, the author is solely responsible for its contents.

1. See Joint Tax Program of the Organization of American States and the Inter-American Development Bank, Fiscal Survey of Colombia (Baltimore: Johns Hopkins Press, 1965), pp. 201-02. For more evidence on the widespread existence in Latin America of complex stamp taxes, see the series of descriptive studies (in Spanish) on Argentina, Chile, Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua published by the Programa Conjunto de Tributación OEA/BID, Union Panamericana, Washington.

subdivided into from ten to twenty smaller groups. In addition, a great many documents must be prepared on stamped paper, and the excise taxes on matches and playing cards are collected by means of stamps. A recent catalog of items and transactions which require stamps or stamped paper lists close to a hundred distinct classes.[2] The list of exempted documents and persons is almost equally complex.

Since stamp taxes and stamped paper originally came into favor mainly for administrative reasons—as a relatively convenient and enforceable way of raising state revenue—it is only fitting that we deal first with some of the administrative problems with the present complex system in the next section. The remainder of the paper consists of a brief economic appraisal of the nature and effects of the Colombian stamp tax and a drastic proposal for its reform.

II. ADMINISTRATIVE ASPECTS

The criteria traditionally applied in public finance treatises to the appraisal of any tax—revenue productivity, simplicity, certainty, convenience of payment, and economic effects—all suggest reforms of the existing stamp tax system.[3]

Table 1 contains some data on the revenue importance of the stamp tax since 1951. Since 1961 when the last major reform took place, stamp tax revenues have remained a fairly constant small proportion of total national government current revenues. Since stamp taxes are imposed on a very broad range of transactions, one might expect, *a priori*, that the yield from this miscellaneous collection of levies would vary more or less in accordance with the level of business activity as indicated by some measure of national income. The elasticity of stamp tax collections to changes in national income in the last fifteen years has been more than unity (that is, stamp taxes have usually increased more in percentage terms than has national income). On this basis a small increase in the relative importance of the stamp tax may perhaps be projected for the next few years, though it is unlikely to return to its 1951 and 1962 peaks (see Table 1). This past performance, however, includes the effects of several important changes in the rates and scope of stamp taxes. Over the long run, with the growing importance of other sources of revenue, stamp tax revenues seem more likely to follow a pattern like that in the United States, where the yield of the stamp taxes fell from 7.4 percent of national revenues in 1916 to only 0.1 percent in 1964.[4] The stamp tax is most unlikely ever to be an important source of revenue in Colom-

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2. See Harvard Law School International Program in Taxation, Taxation in Colombia ("World Tax Series"; Chicago: Commerce Clearing House, Inc., 1964), Chapter 17, pp. 489–504; see also Luis Jimenez Forero and Martín Pinzón Matíz, Timbre Nacional y Papel Sellado (2nd ed.; Bogotá, 1964). The other eleven volumes in the World Tax Series—on Australia, Brazil, India, Mexico, the United Kingdom, Sweden, Italy, France, the Federal Republic of Germany, and the United States—provide ample evidence of the degree to which strictures similar to those outlined in this paper can be applied to the stamp taxes in very different countries.

3. Equity, another traditional criterion, is perhaps not too important in appraising stamp taxes because of their small revenue significance, though the incidence of the system is almost certainly regressive over a broad range of income and regressivity is probably not a very good thing in a country with an income distribution as unequal as Colombia's.

4 See Advisory Commission on Intergovernmental Relations, The Intergovernmental Aspects of Documentary Taxes (Washington, 1964), which recommends the U.S. federal government reduce even further its already very limited use of stamp taxes.

TABLE I

STAMP TAX COLLECTIONS 1951-1965
(millions of pesos)

Year	(b) Stamp Tax	As Percent of Total Current Revenues	As Percent of National Income
1951	45.1	6.7	0.59
1952	25.8	3.7	0.31
1953	29.4	3.5	0.32
1954	34.7	3.3	0.32
1955	35.2	3.1(c)	0.31
1956	51.7	4.5	0.41
1957	55.8	4.5	0.37
1958	59.0	3.6	0.35
1959	73.1	3.8	0.38
1960	84.3	4.0	0.38
1961	128.7	5.8	0.51
1962	140.6	6.6	0.49
1963	168.9	5.2	0.47
1964	227.1	5.4	0.51
1965(a)	234.5	5.3	(d)

(a) Approximate
(b) The 1951-1960 revenue figures incorporate the taxes that were codified in Decree 2908 of 1960; for 1951-56 a special stamp tax on exchange operations has been omitted for greater comparability. These figures are based in part on a study by Dr. Francisco Pineda of the Dirección Nacional del Presupuesto, Ministerio de Hacienda y Crédito Público, Bogotá.
(c) 310 million pesos received from the sale of Paz del Rio shares to the Benco de la República and included as current revenues in 1955 have been omitted from this calculation.
(d) Not available.
Sources: Calculated from data in Contraloría General de la República, Informe Financiero (various years); and in Banco de la República, Cuentas Nacionales (various years).

bia again, whatever its role in the past may have been.

A small revenue yield is not in itself necessarily an argument for abolishing a tax. But when, as appears to be true in the case of the stamp tax, a small yield is combined with a high collection cost, the case for abolition becomes much stronger, since the net change in total revenue will be marginal. Unfortunately, no data are available on the cost to the government of collecting this 5 percent of its current revenues. In 1966, the budgeted cost of merely printing stamps and stamped paper amounted to almost 1 percent of budgeted collections, and the decentralized and complex nature of the distribution system indicates that total collection costs may be very much higher, perhaps four or five times more than for most other national taxes. There can also be no doubt that more was spent in administering such taxes as those on many official activities than was collected from them, since the bulk of the revenue comes from a few taxes.

It is also certain that the "compliance cost," or the cost in time, effort, and money to the taxpayer of obtaining the proper stamps or stamped paper, is a considerable burden on business and personal transactions in Colombia. To cite a common case, the recent legalization of a government contract with a foreign entity involved three visits to a stamp tax vendor for stamps and stamped paper, not to mention a great deal of stamping, cancelling, and counter-signing. The need to get stamps of a particular denomination or so many sheets of stamped paper is always a nuisance and sometimes delays transactions considerably when, for example, there is no stamped paper to be had, or no stamps of the right denomination, as is all too often the case, particularly outside of the capital city, Bogotá.

Though the long tradition behind the system means that the full extent of this compliance burden on both taxpayer and government will probably not be widely realized until it is removed, the fact that the burden is not now much felt—that "an old tax is a good tax"—does not make its existence any more desirable. The only possible argument for the stamp tax as it now exists is that the system gives employment to a good many people, both behind the stamp tax counter and in front of it, thus tending to alleviate Colombia's growing urban unemployment problem. It may be doubted whether this 17th century labor-intensive method of harassing the public constitutes the most useful task to which otherwise idle hands may be put.

The alleged ease of collection (from the government's point of view) and of enforceability of the stamp tax is also more apparent than real. On the one hand, the small revenue yield means that almost no effort has been devoted to enforcing the stamp tax. On the other hand, it is often relatively easy to avoid the tax by changing the form of business arrangements (for example, by booking an air ticket—at the same basic cost—for the route Panamá-Bogotá-Paris) or by misstating values in contracts, or by using fake or no stamps. These practices are especially tempting in the case of ad valorem taxes such as those on air travel (5 percent) and contracts (0.25 percent), though the full impact of the tax can often be avoided simply by stating the value on a contingent basis, in which case only a low fixed tax is payable.

In some countries, such as the United Kingdom,[5] documents that have not been properly stamped are not admissible as evidence in any civil proceeding. Enforcement thus depends on making it in the financial interest of persons dealing with taxable instruments to see that they are properly stamped. In Colombia, as in some other Latin American countries such as Mexico, the basic validity of a document is not impaired by improper stamping, though the authorities are not required to recognize a document as evidence unless it is properly stamped. Since, however, any necessary stamps may be purchased at the time at which the document is put in evidence at a nominal extra cost, this sanction is probably not worth much in practice, although it may at times hamper the enforcement of some contracts. The other penalties (mainly fines of 200–1,000 pesos) do not seem much of a deterrent to evasion either—although the

5. Harvard Law School International Program in Taxation, Taxation in the United Kingdom (Boston: Little, Brown and Company, 1959), pp. 94–104. For a strong administrative argument for modernization and simplification of the British stamp duty system, see "Nuisance of Stamp Duties," Midland Bank Review, May 1959, pp. 3–7.

interest charge on delayed payments of 2.5 percent a month would be worth emulating in the case of other taxes, since in general the interest cost of delaying tax payments has in recent years tended to be negative owing to the accelerated rate of inflation.

On balance, again without real evidence, it seems probable that stamp taxes are often evaded on small transactions and that only nominal tax is often paid on larger ones, when the tax is not completely avoided by changing the form of the transaction, since it is the form and not the fact that is usually the object of taxation. The misuse of the ingenuity of skilled tax practitioners in avoiding taxes in this way is especially to be deplored in a developing country such as Colombia in which capable, trained people are perhaps the scarcest of all resources; of course, this waste is very likely quantitatively greater in the case of other taxes, but this does not redeem the stamp tax.

The complications of the present system of stamp taxes—a conglomeration of taxes and fees imposed partly on capital and partly on transactions and united solely by the fact that the collection of the tax and the proof of its payment is by affixing stamps to a document—are thus plain. It is clear the stamp tax violates any criterion of simplicity or convenience, whether viewed from the point of view of the government or the taxpayer. Furthermore, it is often not at all certain exactly how much stamp tax must be paid on a particular transaction, so that the present system may be said to fall down with regard to certainty also.

In short, on all these essentially administrative grounds, the Colombian stamp tax could use a drastic overhaul and simplification. The exact shape of the recommended changes emerges more clearly from the following brief economic appraisal of some aspects of the present system.

III. AN ECONOMIC APPRAISAL

Some of the existing stamp taxes are really fees, or charges for benefits derived by private persons from government activities. Examples are the taxes on income tax clearance certificates (1 peso), certified copies of documents (various rates), and visas (various rates). In general, it would seem advisable to relate these fees more directly to the cost of providing the service for which the charge is made than is now the case. In some instances, it may even be possible to proportion the charge (which then takes on the characteristics of a benefit tax) more closely to the benefit received by the individual concerned.[6] In many instances, of course, it should be perfectly feasible to charge fees without requiring a stamp to be affixed. Like many techniques of old fiscal administration (for example, the pre-audit of expenditures), the affixing of stamps surely has only a slight deterrent impact on the actual occurrence of fraud, and its very transparency appears in Colombia to have tended to deter any serious effort to discover and treat real cases of evasion.

In some instances, however, it would be better not to charge any fee at all, even when it is easy to do so and when a fair amount of revenue may thus be raised. One example concerns the filing of petitions to the government, a right of the citizen which should presumably not be charged for in a democracy.

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6. This recommendation is made in the Joint Tax Program study cited above; chapter 10 of this study contains a brief analysis of the stamp tax and suggests changes similar to some of those proposed here. The scope for benefit taxation and the charging of fees is in general much wider in most developing countries than is usually thought, despite their characteristically unequal income distributions, in part because much of the benefit from divisible public expenditure tends to accrue to the middle and upper income groups.

Another example concerns the present requirement to pay a 5 peso stamp tax on each of the two copies of the declaration of income required by the income tax law. This provision is clearly regressive in its incidence within the group of income taxpayers: a recent sample study of several thousand income tax returns in Bogota indicated that about one-third of those who file taxable returns (not to mention the even greater number of those who declare income but are exempt from income tax) end up paying more in stamp tax than in income tax—a finding which also indicates the ridiculously low initial rates (starting at 0.5 percent) of the present Colombian income tax. If the administrative saving from handling fewer tax returns is considered more important than the tax consciousness generated by the filing of non-taxable returns, it would be better to set the filing requirement at a higher level (at least equal to the personal exemption) in order to avoid the cost of handling nontaxable returns rather than charging the taxpayer for the privilege of filing as is now done. It is the opposite of logic to levy a charge, even a small one, on an activity such as the filing of income declarations which it is desired to facilitate rather than discourage. There are already too many lines in which a conscientious Colombian taxpayer must stand before complying with his legal duties to justify the addition of yet another before the stamp tax window. A desirable part of any reform of income tax administration would thus be the elimination of the present stamp tax requirement, which was apparently introduced a few years ago to raise some money. The possible argument that most of those who pay little or no income tax should at least pay some stamp tax is without merit; if the income tax is too easy to avoid—as it surely is—the loopholes can and should be easily stopped within the framework of the income tax.

Some parts of the present stamp tax system really are taxes—usually regressive, arbitrary, and easy to avoid taxes, but nevertheless taxes. Some of these taxes are, on the whole, desirable and should be retained. An instance is the 5 percent tax on foreign air travel which could well be raised, since it is both progressive in its incidence and either discourages the spending of so many dollars abroad on travel (through both the substitution and income effects, that is, by making travel relatively more expensive and by reducing income and thus the consumption of almost everything, including travel) or at least ensures that the government receives some compensatory fiscal income when dollars are spent on travel. The exact effect of this tax depends on the largely unknown factors of (a) the elasticity of demand for foreign travel and (b) the ease of avoiding the tax. Other examples might be (according to the Joint Tax Program report) the taxes on mining concessions and the issuance of certain licenses to ships, planes, and firearms dealers.

Some of the existing stamp taxes seem, on the other hand, to be contrary to sensible economic policy and should be eliminated. Conspicuous instances are the tax on public appointments (2 percent, 4 percent, 5 pesos, or some combination) and the tax of 0.2 percent on government payrolls presented for payment. It is so difficult already to hire and keep capable people in the public service that it seems ridiculous to place even minor obstacles in the process. Other examples might be the taxes on credit instruments, checks, and insurance premiums (2.5 to 4 percent), since the government presumably does not want to discourage either saving through insurance or efficient money transfers. A somewhat more complex case concerns the treatment of shares. At present the issuance of new equities is taxed, as is their

transfer. The small transfer tax and the slightly higher issuance tax are probably not too desirable in themselves, though a case can be made for both of them on cost-of-service grounds; but the striking thing is the complete irrationality of the present treatment of bearer shares, the issue of which is taxed at 2 percent of par value compared to 4 percent on registered shares. It seems clear that bearer shares have no rationale for existence except to facilitate tax evasion (whether of the income tax or of the death tax); it is also clear that they cannot be taxed on transfer, whether by a capital gains tax or by a stamp tax, since transfers are not recorded; and it appears difficult politically to abolish them, as would seem logical (and indeed necessary for effective estate or capital gains taxation). A useful compromise might be to levy a very high stamp tax on the issuance of bearer shares: if high enough, this tax would lead to their effective disappearance. Incidentally, the mere existence of stamp taxes on securities transfers (3-5 per cent of value in Colombia) has sometimes been used as an argument against levying a capital gains tax on gains arising from such transaction. This common point has at times received some academic support, at least insofar as the incidence of the stamp tax is on the seller,[7] as it probably is as a rule in Colombia, given the thinness of the securities market. In fact, however, in no sense can the stamp tax really be considered a substitute for a capital gains tax, since it falls on loss transactions also and is not related to either the size of the gain or the income of the recipient. There may be reasons, economic or political, for giving relatively favorable treatment to capital gains realized on securities transactions, but the mere existence of a stamp tax on these transactions is not one of them.[8]

One reason for not taxing stock transactions or real property transfers is that, like any tax on asset transfers, a stamp tax on sales of securities or real property will tend, other things being equal, to lower both the price and volume of traded assets. If it is desired to strengthen the private capital market, both effects seem undesirable in the case of stocks, and the reduction in volume of sales perhaps undesirable in the case of real property. On the other hand, the price-reduction effect on real property would appear to be beneficial. The deterrent to asset transfers exercised by existing Colombian stamp taxes is undoubtedly slight in view of their low rates, but, as Ricardo put it: "For the general prosperity there cannot be too much facility given to the conveyance and exchange of all kinds of property, as it is by such means that capital of every species is likely to find its way into the hands of those who will best employ it in increasing the productions of the country."[9] It would therefore appear that

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7. See Charles Kennedy, "Stamp Duties as a Capital Gains Tax," Review of Economic Studies, XXIII (3), (1955-56), No. 62, pp. 241-44; also Ursula K. Hicks, Development Finance: Planning and Control (Oxford: Clarendon Press, 1965), p. 103. (On the incidence of stamp taxes, see also Carl S. Shoup, "Stamp Duties as a Capital Gains Tax: Comment," Review of Economic Studies, XXV (1), (1957), 53-37.

8. It follows that the replacement of a capital gains tax on sales of securities by a special excise tax—as in Japan in 1953 (see An Outline of Japanese Taxes 1966 (Tax Bureau, Ministry of Finance, 1966), p. 108)—represents a complete change in the character of taxation and cannot be called merely an administrative simplification, as is sometimes done. See also the discussion in n. 9 and the corresponding paragraph in the text.

9. Principles of Political Economy and Taxation (1817) quoted in George F. Break and Ralph Turvey, Studies in Greek Taxation (Research Monograph No. 11, Center of Planning and Economic Research, Athens, 1964), p. 231.

securities transfers should not be taxed by stamp taxes in Colombia, unless the social need for the minor government revenue involved is thought to outweigh the social cost of reducing the volume of stock exchange trading. On balance, even in the absence of empirical evidence, the transfer tax should probably be abolished on stock transfers.

IV. THE PROPOSED REFORM

In conclusion, a list of the specific recommendations for the reform of the present Colombian stamp tax system that emerge from the preceding analysis should be of interest to those entangled in similar systems in other countries:

(1) The stamp tax law should be again consolidated and codified.

(2) Documents that by law should be stamped should have no legal validity unless they are in fact stamped: this suggestion presumes a considerable reduction in the number of documents that have to be stamped and a more effective use and strengthening of the penalties for late or inaccurate stamping.

(3) Stamped paper should be completely abolished, and documentary stamps should be sold through the post office or other available outlets rather than through expensive special vending booths. More care should be taken in the printing and distribution of different stamp denominations to prevent the frequent occurrence of shortages in various parts of the country.

(4) When the tax is really in the nature of a fee for a service provided to a private individual from which he derives a private benefit in excess of the social benefit derived from his taking advantage of the government service, the cost of service is the appropriate basis for the fee. Without some cost studies it is difficult to be precise, but examples of fees that might be set this way are those on the certification and recording of such documents as wills and juridical status. The desirability of paying these fees by means other than stamps should also be carefully examined.

(5) No stamp tax should be levied on income tax declarations or on the filing of petitions to the government.

(6) Stamp taxes should be deductible from the income tax base only to the extent to which their payment is a necessary element in the earning of income, and not, as at present, even when they are connected with such personal expenditures as tourist travel abroad.

(7) The present tax on foreign travel should be raised to at least 15-20 percent and made payable on all tickets purchased by residents within Colombia, no matter what the starting and ending points on the ticket. The administrative difficulties with this proposal are obvious but not insuperable; the political opposition from the articulate users of foreign travel—all of whom always have good reasons for travelling—and from the airlines is probably harder to overcome.

Break and Turvey, Chapter 10, provide a recent clear exposition of the argument against such transfer taxes in developing countries. The weight of this argument in relation to the very strong equity case for capital gains taxes—which would appear to exercise similar "lock-in" effects in many instances—is a complicated question which is not further dealt with here. (See J.G. Head, "The Case for a Capital Gains Tax," Public Finance, XVIII (1963), 220-49, and Richard Goode, The Individual Income Tax (Washington: The Brookings Institution, 1964), Chapter 7, for useful full discussions of capital gains taxes.)

(8) The tax on the issuance of bearer shares should be raised to, say, 50 per cent, and taxes on share transfers abolished.
(9) The taxes on public and private appointments and on payrolls and accounts presented for payment by government employees should be abolished.
(10) The taxes on matches, oils and greases, and playing cards are all nuisance regressive commodity taxes and should be abolished, as should the taxes on insurance policies and on cash transfers and credit instruments, which tend to discourage the development of financial markets.

The immediate net effect of these proposals would probably be to reduce slightly the revenue from stamp taxes (mainly because of the abolition of the tax on income tax declarations), but what is left of the stamp tax system—a few penalty and control taxes and a few fees—should be much more in keeping with the needs of Colombia's increasingly modern economy. It should also be much cheaper to administer and much easier to enforce effectively.

The reform of stamp taxes provides one of the few instances where tax "reform" in Latin America can and should usually mean lower, and certainly fewer, taxes. At the price of at most a very small fall in government revenue an unnecessary and costly wedge can be removed from a vast range of private and public transactions. The social gain from this reform will almost certainly greatly outweigh any small revenue loss that may result.

Further, this small step toward a more modern tax system is as a rule blocked by no political force other than apathy, so that prospects of successful reform, once some attention is directed to the problem, seem high. Virtually every country encumbered with a stamp tax system like Colombia's—and this means most countries—can and should drastically simplify and modernize it along lines similar to those proposed here.

* * * * DOCUMENTS * * * *

L'HARMONISATION DE TAXES SUR LE CHIFFRE D'AFFAIRES DANS LA CEE

directives

Le Conseil de la CEE a arrêté deux directives concernant l'harmonisation de taxes sur le chiffre d'affaires, proposées par la Commission de la CEE.
La première directive contient le principe de la transformation des actuelles taxes en celle de la T.V.A., tandis que la deuxième directive contient la structure et l'application de cette dernière taxe.
Les directives on été acceptées par les Ministres le 9 février 1967 et elles sont arrêtées définitivement le 11 avril 1967 (No. 67/227/CEE et 67/228/CEE).
Les États membres se sont engagés vis à vis du système de la taxe définie dans les directives. Les autorités nationales en arrêteront la forme et les moyens.

NOTE DE L'ÉDITEUR

PREMIÈRE DIRECTIVE DU CONSEIL

du 11 avril 1967

en matière d'harmonisation des législations des États membres relatives aux taxes sur le chiffre d'affaires

LE CONSEIL DE LA COMMUNAUTÉ ÉCONOMIQUE EUROPÉENNE,

vu le traité instituant la Communauté économique européenne, et notamment ses articles 99 et 100,
vu la proposition de la Commission,
vu l'avis de l'Assemblée,
vu l'avis du Comité économique et social,

considérant que l'objectif essentiel du traité est d'établir, dans le cadre d'une union économique, un marché commun comportant une saine concurrence et ayant des caractéristiques analogues à celles d'un marché intérieur; considérant que la réalisation de cet objectif suppose l'application préable, dans les États membres, de législations relatives aux taxes sur le chiffre d'affaires ne faussant pas les conditions de concurrence et n'entravant pas la libre circulation des marchandises et des services dans le marche commun;
considérant que les législations actuellement en vigueur ne répondent pas aux exigences précitées; qu'il est donc dans l'intérêt du marché commun de réaliser une harmonisation des législations relatives aux taxes sur le chiffre d'affaires ayant pour objet l'élimination, dans toute la mesure du possible, des facteurs qui sont susceptibles de fausser les conditions de concurrence, tant sur le plan national que sur le plan communautaire, et permettant d'aboutir par la suite à l'objectif de la suppression des taxations à l'importation et des détaxations à l'exportation pour les échanges entre les États membres;

considérant qu'à la suite des études effectuées, il est apparu que cette harmonisation doit aboutir à l'élimination des systèmes de taxes cumulatives à cascade et à l'adoption par tous les États membres d'un système commun de taxe sur la valeur ajoutée;
considérant qu'un système de taxe sur la valeur ajoutée atteint la plus grande simplicité et la plus grande neutralité lorsque la taxe est perçue d'une manière aussi générale que possible et que son champ d'application englobe tous les stades de la production et de la distribution ainsi que le domaine des prestations de services; qu'il est, par conséquent, dans l'intérêt du marché commun et des États membres d'adopter un système commun dont l'application s'étende également au commerce de détail;
considérant cependant que l'application de la taxe au commerce de détail pourrait se heurter dans quelques États membres à certaines difficultés d'ordre pratique et politique; que, pour cette raison, il faut laisser aux États membres, sous réserve d'une consultation préalable, la faculté de n'appliquer le système commun que jusqu'au stade du commerce de gros inclus et d'appliquer, le cas échéant, au stade du commerce de détail ou au stade antérieur à celui-ci, une taxe complémentaire autonome;
considérant qu'il est nécessaire de procéder par étapes, puisque l'harmonisation des taxes sur le chiffre d'affaires entraînera dans les États membres des modifications considérables de leur structure fiscale et aura des conséquences sensibles dans les domaines budgétaire, économique et social;
considérant que le remplacement des systèmes de taxes cumulatives à cascade en vigueur dans la plupart des États membres par le système commun de taxe sur la valeur ajoutée doit, même si les taux et les exonérations ne sont pas en même temps harmonisés, aboutir à une neutralité concurrentielle, en ce sens qu'à l'intérieur de chaque pays les marchandises semblables supportent la même charge fiscale, quelle que soit la longueur du circuit de production et de distribution, et que, pour les échanges internationaux, le montant de la charge supportée par les marchandises soit connu afin qu'une compensation exacte de cette charge puisse être effectuée; qu'il convient, dès lors, de prévoir, dans une première étape, l'adoption par tous les États membres du système commun de taxe sur la valeur ajoutée, sans harmonisation concomitante des taux et des exonérations;
considérant qu'il n'est pas possible de prévoir dès maintenant de quelle façon et dans quel délai l'harmonisation des taxes sur le chiffre d'affaires peut aboutir à l'objectif de la suppression des taxations à l'importation et des détaxations à l'exportation pour les échanges entre les États membres; qu'il est donc préférable que la deuxième étape ainsi que les mesures à prendre pour cette étape soient déterminées plus tard sur la base des propositions faites par la Commission au Conseil,

A ARRÊTÉ LA PRÉSENTE DIRECTIVE:

Article premier

Les États membres remplacent leur système actuel de taxes sur le chiffre d'affaires par le système commun de taxe sur la valeur ajoutée défini à l'article 2.
Dans chaque État membre la loi ayant pour objet d'effectuer ce remplacement sera promulguée dans les meilleurs délais, afin qu'elle puisse entrer en vigueur à une date qui sera fixée par l'État membre en tenant compte de la situation conjoncturelle, mais qui ne sera pas postérieure au 1er janvier 1970.
A compter de l'entrée en vigueur de cette loi, l'État membre ne peut maintenir ou instituer aucune mesure de compensation for-

faitaire à l'importation ou à l'exportation au titre des taxes sur le chiffre d'affaires pour les échanges entre les États membres.

Article 2

Le principe du système commun de taxe sur la valeur ajoutée, est d'appliquer aux biens et aux services un impôt général sur la consommation exactement proportionnel au prix des biens et des services, quel que soit le nombre des transactions intervenues dans le processus de production et de distribution antérieur au stade d'imposition.

A chaque transaction, la taxe sur la valeur ajoutée, calculée sur le prix du bien ou du service au taux applicable à ce bien ou à ce service, est exigible déduction faite du montant de la taxe sur la valeur ajoutée qui a grevé directement le coût des divers éléments constitutifs du prix.

Le système commun de taxe sur la valeur ajoutée est appliqué jusqu'au stade du commerce de détail inclus.

Toutefois, jusqu'au moment de la suppression des taxations à l'importation et des détaxations à l'exportation pour les échanges entre les États membres, ceux-ci ont, sous réserve de la consultation prévue à l'article 5, la faculté de n'appliquer ce système que jusqu' au stade du commerce de gros inclus et d'appliquer, le cas échéant, au stade du commerce de détail ou au stade antérieur à celui-ci, une taxe complémentaire autonome.

Article 3

Le Conseil arrête, sur proposition de la Commission, une deuxième directive concernant la structure et les modalités d'application du système commun de taxe sur la valeur ajoutée.

Article 4

En vue de permettre au Conseil d'en délibérer et, si possible, de prendre des décisions avant la fin de la période de transition, la Commission soumet au Conseil, avant la fin de l'année 1968, des propositions indiquant de quelle façon et dans quel délai l'harmonisation des taxes sur le chiffre d'affaires peut aboutir à l'objectif de la suppression des taxations à l'importation et des détaxations à l'exportation pour les échanges entre les États membres, en garantissant la neutralité de ces taxes quant à l'origine des biens et des prestations de services.

A cet égard, il doit être tenu compte notamment du rapport entre les impôts directs et indirects, qui diffère selon les États membres, des effets d'une modification des systèmes fiscaux sur la politique fiscale et budgétaire des États membres, ainsi que de l'influence que les systèmes fiscaux exercent sur les conditions de concurrence et sur la situation sociale dans la Communauté.

Article 5

Dans le cas où un État membre envisage d'utiliser la faculté prévue au dernier alinéa de l'article 2, il en saisit la Commission en temps utile et aux fins de l'application de l'article 102 du traité.

Article 6

Les États membres sont destinataires de la présente directive.

Fait à Bruxelles, le 11 avril 1967.

Par le Conseil
Le président
R. VAN ELSLANDE

DEUXIÈME DIRECTIVE DU CONSEIL

du 11 avril 1967

en matière d'harmonisation des législations des États membres relatives aux taxes sur le chiffre d'affaires—Structure et modalités d'application du système commun de taxe sur la valeur ajoutée

LE CONSEIL DE LA COMMUNAUTÉ ÉCONOMIQUE EUROPÉENNE,

vu le traité instituant la Communauté économique européenne, et notamment ses articles 99 et 100,

vu la première directive du Conseil du 11 avril 1967 en matière d'harmonisation des législations des États membres relatives aux taxes sur le chiffre d'affaires,

vu la proposition de la Commission,

vu l'avis de l'Assemblée,

vu l'avis du Comité économique et social,

considérant que le remplacement des taxes sur le chiffre d'affaires en vigueur dans les États membres par un système commun de taxe sur la valeur ajoutée vise à réaliser les objectifs définis par la première directive;

considérant que jusqu'à la suppression des taxations à l'importation et des détaxations à l'exportation, il est possible de laisser aux États membres une large autonomie dans le domaine de la détermination du taux ou des taux différenciés de la taxe;

considérant qu'il est possible également d'admettre à titre transitoire certaines différences dans les modalités d'application de la taxe dans les États membres; qu'il est cependant nécessaire de prévoir des procédures appropriées afin, d'une part, de garantir la neutralité concurrentielle entre les États membres et, d'autre part, de restreindre progressivement ou de supprimer les différences en cause pour aboutir à une convergence des régimes nationaux de taxe sur la valeur ajoutée, afin de préparer la mise en oeuvre de l'objectif visé à l'article 4 de la première directive;

considérant que pour pouvoir appliquer le système de façon simple et neutre et maintenir le taux normal de la taxe dans des limites raisonnables, il est nécessaire de limiter les régimes particuliers et les mesures d'exception;

considérant que le système de taxe sur la valeur ajoutée permet d'opérer, le cas échéant, pour des raisons d'ordre social et économique, des allégements ou des majorations de la charge fiscale sur certains biens et services par une différenciation des taux, mais que l'introduction de taux nuls soulève des difficultés, de sorte qu'il est très souhaitable de limiter strictement les cas d'exonération et de procéder aux allégements estimés nécessaires par l'application de taux réduits d'un niveau assez élevé pour permettre normalement la déduction de la taxe payée au stade précédent, ce qui aboutit d'ailleurs, en général, au même résultat que celui actuellement obtenu par l'application d'exonérations dans les systèmes cumulatifs à cascade;

considérant qu'il est apparu possible de laisser aux États membres le soin de déterminer eux-mêmes la réglementation concernant de nombreuses prestations de services dont le coût n'influe pas sur les prix des biens et le régime à appliquer aux petites entreprises, sous réserve de procéder, en ce qui concerne ce dernier, à une consultation préalable;

considérant qu'il s'est avéré nécessaire de prévoir des régimes spéciaux pour l'application de la taxe sur la valeur ajoutée au secteur agricole et de charger la Commission de soumettre au Conseil, dès que possible, des propositions à cet effet;

considérant qu'il est nécessaire de prévoir un assez grand nombre de dispositions particulières comportant des interprétations, des dérogations et certaines modalités d'application détaillées et d'établir une liste des prestations de services obligatoirement soumises au système commun et qu'il convient de faire figurer ces dispositions et cette liste dans des annexes formant partie intégrante de la présente directive,

A ARRÊTÉ LA PRÉSENTE DIRECTIVE:

Article premier

Les États membres instituent, selon un système commun, une taxe sur le chiffre d'affaires ci-après dénommée «taxe sur la valeur ajoutée». La structure et les modalités d'application de cette taxe sont établies par les États membres selon les dispositions des articles suivants et des annexes A et B.

Article 2

Sont soumises à la taxe sur la valeur ajoutée:
a) les livraisons de biens et les prestations de services, effectuées à titre onéreux à l'intérieur du pays par un assujetti;
b) les importations de biens.

Article 3

Est considéré comme «intérieur du pays», le territoire sur lequel l'État intéressé applique la taxe sur la valeur ajoutée; ce territoire doit englober, en principe, l'ensemble du territoire national, y compris les eaux territoriales.

Article 4

Est considéré comme «assujetti», quiconque accomplit d'une façon indépendante et à titre habituel des opérations relevant des activités de producteur, de commerçant ou de prestataire de services, que ce soit ou non dans un but lucratif.

Article 5

1. Est considéré comme «livraison d'un bien» le transfert du pouvoir de disposer d'un bien corporel comme un propriétaire.

2. Sont également considérées comme une livraison au sens du paragraphe 1:
a) la remise matérielle d'un bien en vertu d'un contrat qui prévoit la location d'un bien pendant une certaine période ou la vente à tempérament d'un bien, assorties de la clause que la propriété est acquise au plus tard lors du paiement de la dernière échéance;
b) la transmission, avec paiement d'une indemnité, de la propriété d'un bien en vertu d'une réquisition faite par l'autorité publique ou en son nom;
c) la transmission d'un bien effectuée en vertu d'un contrat de commission à l'achat ou à la vente;
d) la délivrance d'un travail à façon, c'est-à-dire la remise par l'entrepreneur de l'ouvrage à son client d'un bien meuble qu'il a fabriqué au moyen de matières et objets que le client lui a confiés à cette fin, que l'entrepreneur ait fourni ou non une partie des produits utilisés;
e) la délivrance d'un travail immobilier, y compris celui comportant l'incorporation d'un bien meuble à un bien immeuble.

3. Sont assimilés à une livraison effectuée à titre onéreux:
a) le prélèvement par un assujetti, dans le cadre de son entreprise, d'un bien qu'il affecte à son usage privé ou qu'il transmet à titre gratuit;
b) l'utilisation, par un assujetti pour les besoins de son entreprise d'un bien produit ou extrait par lui ou par un tiers pour son compte.

4. Le lieu de la livraison est réputé se situer:
a) dans le cas où le bien est expédié ou transporté soit par le fournisseur, soit par l'acquéreur, soit par une tierce personne: à l'endroit où le bien se trouve au moment du départ de l'expédition ou du transport à destination de l'acquéreur;
b) dans le cas où le bien n'est pas expédié ou transporté: à l'endroit où le bien se trouve au moment de la livraison.

5. Le fait générateur de la taxe a lieu au moment où la livraison est effectuée. Cependant, pour les livraisons donnant lieu à des versements d'acomptes antérieurement à la livraison, il peut être prévu que le fait générateur ait déjà lieu au moment de la délivrance de la facture ou, au plus tard, au moment de l'encaissement de l'acompte, et ce à concurrence du montant facturé ou encaissé.

Article 6

1. Est considérée comme «prestation de services» toute opération qui ne constitue pas une livraison d'un bien au sens de l'article 5.

2. Les règles prévues dans la présente directive en ce qui concerne la taxation des prestations de services ne sont obligatoirement applicables qu'aux prestations de services qui sont énumérées dans l'annexe B.

3. Le lieu d'une prestation de services est réputé se situer, en principe, à l'endroit où le service rendu, le droit cédé ou concédé ou l'objet loué sont utilisés ou exploités.

4. Le fait générateur de la taxe a lieu au moment où le service est effectué. Cependant, pour les prestations de services à durée indéterminée ou dépassant une certaine période ou donnant lieu à des versements d'acomptes, il peut être prévu que le fait générateur ait déjà lieu au moment de la délivrance de la facture ou, au plus tard, au moment de l'encaissement de l'acompte, et ce à concurrence du montant facturé ou encaissé.

Article 7

1. Est considérée comme «importation d'un bien» l'entrée de ce bien à l'«intérieur du pays» au sens de l'article 3.

2. A l'importation, le fait générateur de la taxe a lieu lors de cette entrée. Toutefois, les États membres ont la faculté de lier le fait générateur et l'exigibilité de la taxe sur la valeur ajoutée au fait générateur et à l'exigibilité prévus en matière de droits de douane ou d'autres impôts, taxes et prélèvements à l'importation.
Le même lien peut être établi en ce qui concerne le fait générateur et l'exigibilité de la taxe sur la valeur ajoutée pour les livraisons de biens importés, placés sous un régime suspensif de droits de douane ou d'autres impôts, taxes et prélèvements.

Article 8

La base d'imposition est constituée:
a) pour les livraisons et prestations de services, par tout ce qui constitue la contre-valeur de la livraison du bien ou de la prestation de services, tous frais et taxes compris à l'exception de la taxe sur la valeur ajoutée elle-même;
b) pour les opérations prévues à l'article 5 paragraphe 3 sous a) et b), par le prix d'achat des biens ou de biens similaires ou, à défaut de prix d'achat, par le prix de revient;
c) pour les importations de biens, par la valeur en douane, majorée de tous les droits, impôts, taxes et prélèvements qui sont dus en raison de l'importation, à l'exception de la taxe sur la valeur ajoutée elle-même.
La même base est applicable lorsque le

bien est exempt de droits de douane ou n'est pas soumis à des droits de douane *ad valorem*.

Chaque État membre a la faculté de majorer la base d'imposition pour les importations de biens des frais accessoires (emballages, transports, assurances, etc.) intervenant jusqu'au lieu de destination et qui ne sont pas compris dans cette base.

Article 9

1. Le taux normal de la taxe sur la valeur ajoutée est fixé par chaque État membre à un pourcentage de la base d'imposition qui est le même pour les livraisons de biens et pour les prestations de services.

2. Certaines livraisons de biens et certaines prestations de services peuvent cependant être soumises à des taux majorés ou à des taux réduits. Chaque taux réduit est fixé de façon telle que le montant de la taxe sur la valeur ajoutée résultant de l'application de ce taux permette normalement de déduire la totalité de la taxe sur la valeur ajoutée dont la déduction est autorisée par l'article 11.

3. Le taux qui doit être appliqué à l'importation d'un bien est celui qui est appliqué à l'intérieur du pays pour la livraison d'un même bien.

Article 10

1. Sont exonérées de la taxe sur la valeur ajoutée, dans les conditions déterminées par chaque État membre:
a) les livraisons de biens expédiés ou transportés en dehors du territoire sur lequel l'État intéressé applique la taxe sur la valeur ajoutée;
b) les prestations de services se rapportant aux biens visés sous a) ou en transit.

2. Peuvent être exonérées de la taxe sur la valeur ajoutée, sous réserve de la consultation prévue à l'article 16, les prestations de services se rapportant à des importations de biens.

3. Chaque État membre peut, sous réserve de la consultation prévue à l'article 16, déterminer les autres exonérations qu'il estime nécessaires.

Article 11

1. Dans la mesure où les biens et services sont utilisés pour les besoins de son entreprise, l'assujetti est autorisé à déduire de la taxe dont il est redevable:
a) la taxe sur la valeur ajoutée qui lui est facturée pour les biens qui lui sont livrés et pour les services qui lui sont rendus;
b) la taxe sur la valeur ajoutée acquittée pour les biens importés;
c) la taxe sur la valeur ajoutée qu'il a acquittée pour l'utilisation de biens visée à l'article 5 paragraphe 3 sous b).

2. N'est pas déductible la taxe sur la valeur ajoutée ayant grevé les biens et les services qui sont utilisés pour effectuer des opérations non imposables, ou exonérées.
L'assujetti est cependant autorisé à opérer la déduction si les livraisons de biens et les prestations de services sont effectuées en dehors du territoire ou exonérées conformément à l'article 10 paragraphe 1 ou 2.
En ce qui concerne les biens et les services qui sont utilisés pour effectuer à la fois des opérations ouvrant droit à déduction et des opérations n'ouvrant pas droit à déduction, la déduction n'est admise que pour la partie de la taxe sur la valeur ajoutée qui est proportionnelle au montant afférent aux premières opérations (règle du prorata).

3. La déduction est opérée sur la taxe sur la valeur ajoutée due pour la période au cours

de laquelle la taxe déductible est facturée dans le cas du paragraphe 1 sous a) ou acquittée dans les cas du paragraphe 1 sous b) et c) (déductions immédiates).
En cas de déduction partielle conformément au paragraphe 2, le montant de la déduction est provisoirement déterminé d'après des critères établis par chaque État membre et régularisé après la fin de l'année lorsque le prorata de l'année de l'acquisition a été calculé.
En ce qui concerne les biens d'investissement, la régularisation est opérée en fonction des variations du prorata intervenues au cours d'une période de cinq années, dont celle au cours de laquelle les biens ont été acquis; elle ne porte chaque année que sur un cinquième de la taxe dont les biens d'investissement ont été grevés.

4. Peuvent être exclus du régime des déductions, certains biens et certains services, notamment ceux qui sont susceptibles d'être exclusivement ou particllement utilisés pour les besoins privés de l'assujetti ou de son personnel.

Article 12

1. Tout assujetti doit tenir une comptabilité suffisamment détaillée pour permettre l'application de la taxe sur la valeur ajoutée et les contrôles par l'administration fiscale.

2. Tout assujetti doit délivrer une facture pour les livraisons de biens et les prestations de services qu'il a effectuées à un autre assujetti.

3. Tout assujetti doit déposer chaque mois une déclaration indiquant pour les opérations effectuées au cours du mois précédent tous les renseignements nécessaires pour le calcul de la taxe et des déductions à opérer. Tout assujetti doit verser le montant de la taxe sur la valeur ajoutée lors du dépôt de la déclaration.

Article 13

Si un État membre estime que, dans des cas exceptionnels, il y a lieu d'instaurer des mesures particulières, afin de simplifier la perception de la taxe ou d'éviter certaines fraudes, il en informe la Commission et les autres États membres.
S'il y a opposition d'un ou de plusieurs États ou de la Commission dans le délai d'un mois, la demande de dérogation est portée devant le Conseil qui statue sur proposition de la Commission dans un délai de trois mois.
S'il ressort des conclusions de la Commission qu'il s'agit seulement d'une simplification de la perception ou d'une mesure destinée à éviter la fraude, le Conseil statue à la majorité qualifiée sur la dérogation demandée.
S'il ressort au contraire desdites conclusions que la mesure envisagée risque de porter atteinte aux principes mêmes du régime institué par la présente directive, et notamment à la neutralité concurrentielle entre les États membres, le Conseil statue à l'unanimité.
Dans l'un et l'autre cas, le Conseil statue selon les mêmes modalités sur la durée d'application de ces mesures.
L'État intéressé ne peut mettre en application les mesures envisagées qu'a l'expiration du délai d'opposition ou, lorsqu'il y a eu opposition, d'après la décision du Conseil, si celle-ci est favorable.
Ces dispositions cesseront d'être applicables lors de la suppression des taxations à l'importation et des détaxations à l'exportation pour les échanges entre les États membres.

Article 14

Chaque État membre a la faculté, sous réserve de la consultation prévue à l'article 16, d'appliquer aux petites entreprises, pour lesquelles l'assujettissement au régime normal

de la taxe sur la valeur ajoutée se heurterait à des difficultés, le régime particulier qui s'adapte le mieux aux exigences et possibilités nationales.

Article 15

1. La Commission soumet au Conseil, dans les meilleurs délais, des propositions de directives concernant les modalités communes d'application de la taxe sur la valeur ajoutée aux opérations portant sur les produits agricoles.

2. Jusqu'à la date fixée dans les directives visées au paragraphe 1 pour la mise en application de ces modalités communes, chaque État membre a la faculté, sous réserve de la consultation prévue à l'article 16, d'appliquer aux exploitants agricoles, pour lesquels l'assujettissement au régime normal de la taxe sur la valeur ajoutée se heurterait à des difficultés, le régime particulier qui s'adapte le mieux aux exigences et possibilités nationales.

Article 16

Dans les cas où un État membre doit, d'après les dispositions de la présente directive, procéder à des consultations, il saisit la Commission en temps utile et aux fins de l'application de l'article 102 du traité.

Article 17

En vue du passage des systèmes actuels de taxes sur le chiffre d'affaires au système commun de taxe sur la valeur ajoutée, les États membres ont la faculté:
– de prendre des dispositions transitoires pour percevoir la taxe par anticipation;
– d'appliquer, pendant une certaine période transitoire, pour les biens d'investissement, la méthode de déductions selon des fractions annuelles (déductions *prorata temporis*);
– d'exclure, pour une certaine période transitoire, totalement ou partiellement, les biens d'investissement du régime des déductions prévu à l'article 11;
et, sous réserve de la consultation prévue à l'article 16:
– d'autoriser, afin d'accorder une décharge, totale ou partielle, mais de portée générale, de la taxe sur le chiffre d'affaires perçue jusqu'au moment de la mise en application de la taxe sur la valeur ajoutée, des déductions forfaitaires pour les biens d'investissement non encore amortis ainsi que pour les stocks existant au même moment. Toutefois, les États membres ont la faculté de restreindre ces déductions aux biens exportés pendant une période d'un an à compter de la mise en application de la taxe sur la valeur ajoutée. Dans ce cas, ces déductions ne pourront être accordées que pour les biens existant en stock au moment précité et exportés en l'état;
– de prévoir, jusqu'au moment de la suppression des taxations à l'importation et des détaxations à l'exportation pour les échanges entre les États membres, pour des raisons d'intérêt social bien définies et en faveur des consommateurs finals, des taux réduits ou même des exonérations avec remboursement éventuel des taxes payées au stade antérieur, dans la mesure où l'incidence globale de ces mesures ne dépasse pas celle des allégements appliqués dans le régime actuel.

Article 18

La Commission présente au Conseil, après consultation des États membres, pour la première fois le 1er janvier 1972 et ensuite tous les deux ans, un rapport sur le fonctionnement du système commun de taxe sur la valeur ajoutée dans les États membres.

Article 19

Le Conseil, dans l'intérêt du marché commun, adopte le moment venu, sur proposition de la Commission, les directives appropriées en vue de compléter le système commun de taxe sur la valeur ajoutée et, notamment, de restreindre progressivement ou de supprimer les mesures prises par les États membres en dérogation de ce système, pour aboutir à une convergence des régimes nationaux de taxe sur la valeur ajoutée, afin de préparer la mise en oeuvre de l'objectif visé à l'article 4 de la première directive.

Article 20

Les annexes font partie intégrante de la présente directive.

Article 21

Les États membres sont destinataires de la présente directive.

Fait à Bruxelles, le 11 avril 1967.

Par le Conseil
Le président
R. VAN ELSLANDE

ANNEXE A

1. Ad article 3

Si un État membre envisage d'appliquer la taxe sur la valeur ajoutée sur un territoire plus restreint que son territoire national, il procède à la consultation prévue à l'article 16.

2. Ad article 4

Le terme «activités de producteur, de commerçant ou de prestataire de services» doit être entendu dans un sens large et englober l'ensemble des activités économiques y compris, par conséquent, les activités extractives, les activités agricoles et celles des professions libérales.

Si un État membre envisage de ne pas imposer certaines activités, il convient qu'il le fasse au moyen d'exonérations plutôt q'en excluant du champ d'application de la taxe les personnes exerçant ces activités.

Les États membres ont la faculté de considérer également comme «assujetti» quiconque accomplit les opérations visées par l'article 4 à titre occasionnel.

Le terme «d'une façon indépendante» vise notamment à exclure de la taxation les salariés qui sont liés à leur employeur par un contrat de louage de travail. Ce terme permet également à chaque État membre de ne pas considérer comme des assujetti séparés, mais comme un seul assujetti, les personnes qui, bien qu'indépendantes du point de vue juridique, sont cependant organiquement liées entre elles par des rapports économiques, financiers et d'organisation. L'État membre qui envisage d'adopter un tel régime, procède à la consultation prévue à l'article 16.

Les États, les provinces, les communes et les autres collectivités de droit public ne sont pas considérés, en principe, comme des assujettis pour les activités qu'ils exercent en tant qu'autorités publiques.

Toutefois, s'ils exercent des activités de producteur, de commerçant ou de prestataire de services, ils peuvent être considérés comme des assujettis pour ces activités.

3. Ad article 5 paragraphe 1

Par «bien corporel» il faut entendre les biens corporels, tant meubles qu'immeubles.

Les livraisons de courant électrique, de gaz,

de chaleur, de froid et de choses similaires sont considérées comme des livraisons de biens.
Les États membres ont la faculté de considérer qu'en cas d'apport à une société d'une universalité totale ou partielle de biens, la société bénéficiaire est censée continuer la personne de l'apporteur.

4. Ad article 5 paragraphe 2 sous a)
Pour l'application de la présente directive, le contrat visé à l'article 5 paragraphe 2 sous a) ne doit pas être décomposé pour partie en une location et pour partie en une vente, mais être considéré, dès sa conclusion, comme un contrat comportant une livraison imposable.

5 Ad article 5 paragraphe 2 sous d) et e)
Les États membres qui, pour des raisons spécifiquement nationales, ne pourraient pas considérer les opérations visées à l'article 5 paragraphe 2 sous d) et e) comme des livraisons, devront les ranger dans la catégorie des prestations de services en les soumettant au taux qui leur serait applicable si elles étaient considérées comme des livraisons.
Sont considérés entre autres comme «travaux immobiliers»:
– la construction de bâtiments, ponts, routes, ports, etc., en exécution d'un contrat de louage d'ouvrage;
– les travaux de terrassement et plantations de jardins;
– les travaux d'installation (de chauffage central, par exemple);
– les réparations portant sur des immeubles, autres que les opérations d'entretien courant.

6. Ad article 5 paragraphe 3 sous a)
En ce qui concerne le prélèvement en l'état d'un bien acheté par un assujetti, les États membres ont la faculté de remplacer l'imposition par l'interdiction de la déduction ou par sa régularisation si la déduction a déjà été opérée. Cependant, les prélèvements effectués pour donner des cadeaux de faible valeur et des échantillons qui, fiscalement, peuvent être rangés parmi les frais généraux, ne doivent pas être considérés comme livraisons imposables. De plus, les dispositions prévues à l'article 11 paragraphe 2 ne sont pas applicables à de tels prélèvements.

7. Ad article 5 paragraphe 3 sous b)
Cette disposition ne doit être appliquée que pour assurer une égalité de taxation entre les biens achetés et destinés aux besoins de l'entreprise et n'ouvrant pas droit à une déduction immédiate ou complète, d'une part, et les biens produits ou extraits par l'assujetti ou pour son compte par un tiers et également utilisés pour les mêmes besoins, d'autre part.

8. Ad article 5 paragraphe 5
Par «fait générateur de la taxe» il faut entendre la naissance de la dette fiscale.

9. Ad article 6 paragraphe 1
La définition de la prestation de services donnée dans ce paragraphe implique qu'il faut ranger, entre autres, parmi les prestations de services:
– la cession d'un bien incorporel;
– l'exécution d'une obligation de ne pas faire quelque chose;
– l'exécution d'un service rendu en vertu d'une réquisition faite par l'autorité publique ou en son nom;
– l'exécution d'un travail portant sur un bien, si ce travail n'est pas considéré comme une livraison au sens de l'article 5 paragraphe 2 sous d) et e) comme, par exemple, les opérations d'entretien courant, le blanchissage du linge, etc.
Cette définition ne s'oppose pas à la taxation par les États membres de certaines opérations

effectuées par un assujetti comme des services «rendus à soi-même», lorsqu'une telle mesure s'avère nécessaire pour éviter des distorsions de concurrence.

10. Ad article 6 paragraphe 2
Les États membres s'abstiennent, dans toute la mesure du possible, d'exonérer les prestations de services énumérées à l'annexe B

11. Ad article 6 paragraphe 3
Le Conseil, statuant à l'unanimité sur proposition de la Commission, arrête, avant le 1er janvier 1970, des dispositions spéciales concernant certaines prestations de services pour lesquelles elles s'avéreraient nécessaires, en dérogeant éventuellement aux dispositions de l'article 6 paragraphe 3. Jusqu'à ce que ces dispositions aient été arrêtées, chaque État membre a la faculté, en vue de simplifier la perception de la taxe, de déroger aux dispositions de l'article 6 paragraphe 3, en prenant toutefois les dispositions utiles pour éviter la double imposition ou la non-imposition.

12. Ad article 8
L'État membre qui n'applique la taxe sur la valeur ajoutée que jusqu'au stade du commerce de gros inclus peut, dans le cas de biens vendus au détail par un assujetti, réduire la base d'imposition d'un certain pourcentage; toutefois, la base ainsi réduite ne peut être inférieure au prix d'achat ou de revient, majoré, le cas échéant, du montant des droits de douane (y compris les prélèvements), impôts et taxes à la charge du bien, même si le paiement en a été suspendu, à l'exception de la taxe sur la valeur ajoutée.
En cas d'importation d'un bien vendu au détail, une même réduction doit être appliquée à la base d'imposition.
Il est laissé aux États membres le soin de définir, d'après leur conception nationale, la notion de «vente de biens au détail».
Chaque État membre a, sous réserve de la consultation prévue à l'article 16, la faculté de prévoir, à titre de mesure préventive de la fraude et pour des biens et des services limitativement désignés, que, par dérogation à l'article 8, la base d'imposition ne peut être inférieure à une base minimum fixée dans la législation nationale.

13. Ad article 8 sous a)
Par le mot «contre-valeur» il faut entendre tout ce qui est reçu en contrepartie de la livraison du bien ou de la prestation de services, y compris les frais accessoires (emballages, transports, assurances, etc.), c'est-à-dire non seulement le montant des sommes perçues, mais aussi, par exemple, la valeur des biens reçus en échange ou, dans le cas de réquisition faite par l'autorité publique ou en son nom, le montant de l'indemnité perçue.
Toutefois, cette disposition ne s'oppose pas à la faculté pour chaque État membre qui l'estime nécessaire pour aboutir à une neutralité concurrentielle plus grande, d'exclure de la base d'imposition pour les livraisons les frais accessoires intervenus à partir du lieu de la livraison défini à l'article 5 paragraphe 4 et de taxer ces frais comme la contre-valeur d'une prestation de services.
Cependant, les frais payés au nom et pour le compte du client et qui sont portés dans la comptabilité du fournisseur dans des comptes de passage, ne constituent pas un élément de la base d'imposition.
Les droits de douane et autres taxes, impôts, etc., payés à l'importation par des agents et autres intermédiaires en douane y compris les expéditeurs, sous leur propre nom, peuvent également être exclus de la base d'imposition correspondant à la prestation de services qu'ils ont fournis.

14. Ad article 8 sous c)
Dans les échanges intracommunautaires, les

États membres s'efforceront d'appliquer aux importations de biens une base d'imposition qui corresponde, dans toute la mesure du possible, à celle qui est retenue pour les livraisons effectuées à l'intérieur du pays, cette base comprenant les mêmes éléments que ceux pris en compte en vertu de l'article 8 sous c).

Au plus tard jusqu'à la suppression des taxations à l'importation et des détaxations à l'exportation pour les échanges entre les États membres et sous réserve de la consultation prévue à l'article 16, chaque État membre a la faculté d'appliquer aux importations de biens en provenance des pays tiers, une base d'imposition qui corresponde, dans toute la mesure du possible, à celle qui est retenue pour les livraisons effectuées à l'intérieur du pays, cette base comprenant les mêmes éléments que ceux pris en compte en vertu de l'article 8 sous c).

15. Ad article 9 paragraphe 2

Dans la mesure où il est fait usage des dispositions de ce paragraphe pour les prestations de transport visées dans l'annexe B point 5, elles doivent être appliquées de façon à assurer l'égalité de traitement entre les différents modes de transport.

16. Ad article 10 paragraphe 1 sous a)

L'exonération prévue dans cette disposition vise la livraison d'un bien qui est directement exporté, c'est-à-dire la livraison effectuée par l'exportateur. Les États membres ont toutefois la faculté d'étendre l'exonération aux livraisons effectuées au stade précédent.

17. Ad article 10 paragraphe 1 sous b)

Toutefois, les États membres ont la faculté de renoncer à cette exonération si la décharge de la taxe sur la valeur ajoutée ayant frappé ces prestations de services est réalisée auprès du bénéficiaire de ces prestations par voie de déductions. De plus, les États membres ont la faculté, excepté pour les prestations de services se rapportant aux biens en transit, de limiter cette exonération aux prestations de services qui se rapportent à des biens dont la livraison à l'intérieur du pays est imposable.

18. Ad article 10 paragraphe 2

Cette disposition vise, notamment, les prestations de transports internationaux à l'importation et les services portuaires.

19. Ad article 10 paragraphes 2 et 3

Dans la mesure où il est fait usage des dispositions de ces paragraphes pour les prestations de transport visées dans l'annexe B point 5, elles doivent être appliquées de façon à assurer l'égalité de traitement entre les différents modes de transport.

20. Ad article 11 paragraphe 1 sous a)

Dans les cas prévus à l'article 5 paragraphe 5 deuxième phrase et à l'article 6 paragraphe 4 deuxième phrase, les déductions peuvent être appliquées dès réception de la facture, alors même que les biens ne sont pas encore livrés ou que les services ne sont pas encore rendus.

21. Ad article 11 paragraphe 2 deuxième alinéa

Toutefois, les États membres ont la faculté de limiter le droit à déduction aux opérations se rapportant à des biens dont la livraison à l'intérieur du pays est imposable.

22. Ad article 11 paragraphe 2 troisième alinéa

Le prorata est en principe déterminé pour l'ensemble des opérations effectuées par l'assujetti (prorata général). Cependant, un assujetti peut obtenir exceptionnellement l'autorisation administrative de déterminer des prorata spéciaux pour certains secteurs de son activité.

23. Ad article 11 paragraphe 3 premier alinéa
Sous réserve de la consultation prévue à l'article 16, chaque État membre a la faculté, pour des raisons conjoncturelles, d'exclure partiellement ou totalement du régime des déductions les biens d'investissement ou d'appliquer pour ces biens au lieu de la méthode des déductions immédiates celle des fractions annuelles (déductions *prorata temporis*).

24. Ad article 11 paragraphe 3 troisième alinéa
Les États membres ont la faculté de fixer certaines tolérances pour limiter le nombre des régularisations en cas de variation du prorata annuel par rapport au prorata initial qui a servi de base à la déduction pour les biens d'investissement.

25. Ad article 12 paragraphe 2
La facture doit mentionner, d'une façon distincte, le prix hors taxe et la taxe correspondante pour chaque taux différent, ainsi que, le cas échéant, l'exonération.
Chaque État membre peut prévoir, dans des cas spéciaux, des dérogations à cette disposition ainsi qu'à l'obligation prévue à l'article 12 paragraphe 2. Toutefois, ces dérogations doivent être strictement limitées.
Nonobstant les autres mesures à prendre par États membres pour assurer le paiement de la taxe et éviter les fraudes, toute personne, assujettie ou non, qui mentionne la taxe sur la valeur ajoutée sur une facture est tenue d'en acquitter le montant.

26. Ad article 12 paragraphe 3
Chaque État membre a la faculté, pour des raisons pratiques, de raccourcir le délai prévu à l'article 12 paragraphe 3 ou d'autoriser certains assujettis à déposer la déclaration pour chaque trimestre, semestre ou année.
Au cours du premier semestre de chaque année, l'assujetti doit déposer, le cas échéant, une déclaration concernant toutes les opérations effectuées l'année précédente et comportant tous les éléments nécessaires aux régularisations éventuelles.
Pour les importations des biens, les modalités de la déclaration et du paiement qui doit s'ensuivre font l'objet de dispositions qui sont arrêtées par chaque État membre.

27. Ad article 14
Dans la mesure où il est fait usage des dispositions de cet article pour les prestations de transport visées dans l'annexe B point 5, elles doivent être appliquées de façon à assurer l'égalité de traitement entre les différents modes de transport.

28. Ad article 17 quatrième tiret
L'évaluation des stocks peut être faite notamment par référence aux opérations effectuées par les assujettis au cours des années précédentes.

ANNEXE B

Liste des prestations de services visées à l'article 6 paragraphe 2

1. Les cessions de brevets, de marques de fabrique et de commerce et d'autres droits similaires, ainsi que les concessions de licences concernant ces droits;

2. Les travaux autres que ceux visés à l'article 5 paragraphe 2 sous d), portant sur des biens corporels meubles et exécutés pour un assujetti;

3. Les prestations tendant à préparer ou à coordonner l'exécution de travaux immobiliers comme, par exemple, les prestations fournies par les architectes et les bureaux de surveillance de travaux;

4. Les prestations de publicité commerciale;

5. Le transport de biens et le magasinage de biens, ainsi que les prestations accessoires;

6. La location de biens corporels meubles à un assujetti;

7. La fourniture de personnel à un assujetti;

8. Les prestations fournies par les conseillers, les ingénieurs, les bureaux de planning et les prestations similaires, dans les domaines technique, économique ou scientifique;

9. L'exécution d'une obligation de ne pas exercer, entièrement ou partiellement, une activité professionnelle ou un droit visé dans la présente liste;

10. Les prestations des expéditeurs, courtiers, agents d'affaires et autres intermédiaires autonomes, pour autant qu'elles portent sur les livraisons ou importations de biens ou sur les prestations de services énumérées dans la présente liste.

CHRONOLOGY OF THE COMMON MARKET

Ten years of the Treaty of Rome

On the occasion of the tenth anniversary of the signing of the Treaty of Rome, which established the European Economic Community, the Official Spokesman of the Commission considers to draw up a brief chronological review of the most important achievements and salient events of this period of the Community's activity, beginning at January 1958.
Obviously, this review cannot claim to be exhaustive; the aim is, rather, to provide a practical outline that will enable readers to see at a glance how far the Community institutions and the Member States have come in their constant and tireless effort to achieve European integration.

JANUARY 1958 – FEBRUARY 1967

1958

During this year, which marked the beginning of the 12-year transition period leading to the common market, the institutions of the European Economic Community were established and began to operate.

The Treaty of Rome, which had been signed in Rome on 25 March 1957, entered into force on 1 January. The members of the European Commission were appointed by the representatives of the Governments of the Member States meeting in Paris on 6 and 7 January. The EEC Commission established its headquarters in Brussels, where it met for the first time at the Château de Val-Duchesse on 16 January; throughout the year it was occupied with the progressive establishment of its various departments. The inaugural meeting of the Council of Ministers took place on 25 and 26 January.

The European Parliamentary Assembly, which exercises powers of control over the High Authority, the Common Market Commission and the Euratom Commission, enlarged its membership from 78 to 142. It held its first session in Strasbourg from 19 to 21 March.

In pursuance of Article 43 of the Treaty, the Commission called a conference of the Member States at Stresa in order to confront and compare their agricultural policies. This conference, which took place from 3 to 11 July, was the first step towards the elaboration of the common agricultural policy.

On 7 October, the Court of Justice of the three Communities, which sits at Luxembourg, replaced the Court of Justice of the ECSC.

1 January	– Entry into force of the Treaties of Rome, signed on 25 March 1957, establishing the European Economic Community and Euratom.
7 January	– Members of the Commission appointed by the Conference of the six Foreign Ministers of the European Community. M. Walter Hallstein appointed President of the EEC Commission.
16 January	– First meeting of the Commission.
25-26 January	– Inaugural meeting of the EEC Council.

3 February – Mr. Walter Butterworth, Head of the US Mission, accredited. He is the first representative of a non-member country to the EEC.
13 March – The Commission issues its first regulation.
19–21 March – First session of the European Parliamentary Assembly, later called European Parliament. M. Robert Schuman elected President.
20 April – First issue of official gazette, replacing official gazette of the ECSC.
3–12 July – Confrontation of national agricultural policies at Stresa, with a view to the elaboration of the common agricultural policy.
19 July – Opening of a European school in Brussels decided by the Board of Governors of the European School in Luxembourg.
25 September and 3 December – Adoption by the Council of the first regulations on social security of migrant workers.
2–3 December – Council Regulations Nos. 5 and 6 on the European Development Fund (EDF) for associated overseas countries and territories.
3–4 December – The Council decides on a 10% unilateral tariff reduction towards GATT members and offers to increase the volume of its quotas by 20% on condition of reciprocity.
15 December – The OEEC Council notes the disagreement of member countries on the British proposals to establish a European free trade zone.

1959

This year saw the first concrete results. On 1 January the first 10% cut was made in the duties on industrial products in trade between Member States. This reduction also applied to trade between the Six and the overseas and territories associated with the Community (OCT), as well as to trade between the OCT in cases where preferential customs tariffs had been in force.
At the same time, preparations were made for a large number of measures to harmonize the rules of competition in the Common Market, and the Commission worked out its first proposals for common economic policies, particularly in the agricultural sphere. While the common customs tariff was being elaborated, non-member countries reacted to the EEC's appearance on the international scene. In the middle of the year, Greece asked for a treaty of association, and shortly afterwards Turkey did likewise. The establishment of the European Free Trade Association was announced on 20 November, its members being Austria, Denmark, Norway, Portugal, Sweden, Switzerland and the United Kingdom.
The EDF financed 60 development projects estimated at 40 million u.a. for the benefit of associated overseas countries.

1 January – First tariff reductions and first quota increases.
27 January – Establishment of the Consultative Committee on Transport.
23 February – Commission Regulation No. 7 governing the administration of the EDF.
27 February – The Commission presents a memorandum stressing that relations with European countries must be viewed in the framework of a worldwide general policy.

25 May – Creation of an Inter-executive Working Party on energy.
8 June – Greece applies for association.
16 July – First Conference of Ministers of Finance of the Six.
31 July – Turkey applies for association.
7 November – The Council decides to offer GATT, on a basis of reciprocity, erga omnes treatment for quota measures and certain tariff reductions for industrial products.
– The Commission transmits to the Economic and Social Committee its proposals on the formulation and execution of the common agricultural policy.
20 November – Establishment of the European Free Trade Association; members: Austria, Denmark, Norway, Portugal, Sweden, Switzerland and the United Kingdom.
23 November – The Council adopts the first directive on arrangements for progressive exercise of the right of establishment in the Overseas Countries and Territories and Overseas Departments.

1960

The outstanding event of the year was the decision, taken by the Six in May, to speed up the development of the common market as from the following year. This had been made possible by the vigorous expansion of the economy. Intra-Community trade went up by 50% from 1958 to 1960, while the increase in imports from non-member countries, although somewhat smaller, was nevertheless considerable.

In all fields, the Community's activities expanded. Acting on a proposal from the Commission, the Council approved the basic principles for a common competition policy in February, and those for a common agricultural policy in November.

The first measures on the free movement of capital were adopted in May. The Social Fund, which repays to the Member States half of the expenditure they incur in fitting reduntant workers for others jobs, came into operation in August.

In July, tariffs were cut for the second time, as laid down by the Treaty. The duty on each product was reduced to 80% of the original duty. The common customs tariff had been adopted by the Council of Ministers in February.

At Geneva, the Commission was engaged in negotiations in GATT which were to lead, in 1961, to recognition of its customs tariff by the Contracting Parties.

The EDF financed 61 developments projects in associated countries to a total of 73 million u.a.

February – The Commission puts to the Council the broad lines of a competition policy in the Community.
13 February – The common customs tariff is adopted by the Council.
26 February – Commission recommendation to the Council on speeding up the implementation of the Treaty.
2 March – Common customs tariff adopted for List G products by a conference of representatives of the Member States held in Rome.

7 April – First meeting of the Short-term Economic Policy Committee set up by the Council at the beginning of February.

12 May – First measures to speed up tariff disarmament between the Member States decided by the Council.
– Adoption by the Council of the first directive for the implementation of Article 67 of the Treaty on the free movement of capital.

27 June – The Council adopts the first transport regulation: abolition of discrimination in transport rates and conditions.

30 June – Final text of the Commission's proposals for a common agricultural policy submitted to the Council.

20 July – The Council sets up the Special Committee for Agriculture.
– Council decision on the insertion of an EEC Clause in bilateral trade agreements.

25 August – Regulation on the operation of the European Social Fund adopted by the Council.

1 September – Opening in Geneva of re-negotiations on national tariffs of Member States (GATT Article 24, 6).

12 November – Commission memorandum on the applicability to transport of competition rules and on the interpretation and application of the Treaty in respect of shipping and air transport.

15 November – First decisions taken by the Council on the principles of the common agricultural policy.

21-22 November – The political groups in the European Parliament declare themselves in favour of the merger of the executives.

20 December – Agreement of the Council that the provisions concerning faster progress in the field of trade in agricultural products will be applicable from 1 January 1961. Resolution adopted on the principles to be taken as a basis for a system of levies on certain products to be determined.

1961

The provisions for faster tariff disarmament entered into force. On 1 January customs duties on industrial products were reduced to 70% of the original duty, and thise on non-liberalized agricultural products to 75%.
Introduction of the common customs tariff was also speeded up. The first alignment of national tariffs took place on 1 January—one year earlier than originally planned.
In July the Council of Ministers ratified the tariff agreements that had been reached with 17 countries at negotiations in Geneva arising from the progressive replacement of national duties by the common tariff.

Common policies were also an important feature of the year's work. At the end of June the Commission's proposals on the common agricultural policy were laid before the Council in their final form. Two months earlier the Commission had submitted a memorandum to the Council on the main lines of a common transport policy.
The first joint proposals for a co-ordinated energy policy were presented to the Governments by the EEC Commission, the High Authority and the Euratom Commission.
In December the Council, acting on a proposal from the Commission, adopted a general

programme for the introduction of freedom of establishment and freedom to supply services. It also adopted an initial regulation on cartels and dominant positions, thus laying the foundations of a European anti-trust legislation based on Articles 85 and 86 of the Treaty of Rome. In August the first regulation on the free movement of workers in the Member States was adopted in pursuance of Articles 48 and 49 of the Treaty.

Where external relations were concerned, the year brought the signature of the Association Agreement between the EEC and Greece, and the opening of negotiations with the United Kingdom which had applied for membership of the Community. Similar applications were made by Denmark and Ireland, while Austria, Switzerland, Sweden and Spain applied for association with the Community.

The EDF financed 100 projets in the associated overseas countries to a total of 137 million u.a.

1 January – First alignment of national tariffs towards the CCT.

10 January – Proposal by the Inter-executive Working Party to the six Governments for certain initial measures of common energy policy.

10 April – Commission Memorandum on the general lines of a common transport policy.

29 May – Opening in Geneva of the multilateral phase of the tariff conference (Dillon round). The EEC offers a 20% across-the board cut on industrial products.

19–24 June – First EEC/AASM Parliamentary Conference in Strasbourg.

9 July – Signing of the Association Agreement with Greece.

12 July – Commission memorandum on the future EEC-AASM Association.

31 July – Ireland applies for membership of the EEC.

9 August – The United Kingdom applies for membership of the EEC after a declaration by Mr. Macmillan in the House of Commons on 31 July.

10 August – Denmark applies for membership of the EEC.

16 August – The first regulation in pursuance of Articles 48 and 49 of the Treaty, concerning the free movement of workers, is adopted by the Council.

28 September –4 October – Consultative conference with trade organizations in Rome on the social aspects of the common agricultural policy.

9 October – Council decision on harmonization of the duration of trade agreements with non-member countries.

8 November – Opening of negotiations between the EEC and the United Kingdom.

6–7 December – First meeting of the Council and the ministers of the associated African states to decide upon the basic principles of the new Convention of Association.

15 December – Austria, Sweden and Switzerland apply for association with the EEC.

21 December – The Council adopts the General Programmes to introduce freedom of establishment and freedom to supply services.

1962

After protracted discussions which ended on 14 January, the second stage of the transition period opened with the adoption of the first regulations on common agricultural policy,

which replaced the highly complicated legislation of the Member States. These first regulations came into force in August; they established a common organization of the markets in cereals, pigmeat, eggs, poultrymeat, wine, and fruit and vegetables.
The dismantling of internal tariffs continued. Two reductions were made, one on 1 January as provided for by the Treaty, and the other on 1 July following decisions to speed up tariff disarmament. The original duties on industrial products had now fallen by half. In Geneva, the Community and the United States granted each other fresh tariff concessions covering a total volume of trade of some $ 1 600 m. in both directions. The Community reduced the CCT duties by 20% for products of which the United States was the chief supplier.
The Council decided that equal pay for men and women should be introduced in three stages by the end of 1964.
The Commission continued its work on common polices. In May it submitted to the Council a programme to establish a common transport system, and in September the Council approved the first programme for the progressive harmonization of the Member States' commercial policies.
On a broader plane, the Commission drew up an "action programme" for the Community during the second stage, which it published in October; the emphasis was laid on progressive merging of the Member States' economic policies into a common policy both for the short and for the long term.
In September the association of Surinam with the Community entered into force.
The EDF financed 83 development projects in associated overseas countries to a total of 169 million u.a.

14 Januari
- Agreement on the broad lines of the common agricaltural policy (notably six regulations on market organizations; establishment of the Guidance and Guarantee Fund; rules of competition applicable to agricultural products) and opening of the second stage of the transition period, with effect from 1 January.
- Adoption by the Council of the first regulation on cartels (No. 17).

9 February
- Spain applies for association with the EEC.

21 March
- The Council decides to institute prior examination and consultation procedure in respect of legislation contemplated by the Member States in the sphere of transport.

30 April
- Norway applies for membership of the EEC.

15 May
- Second decision by the representatives of the Member States meeting in the Council to speed up tariff disarmament among the Six.
- The Council approves the consultation procedure recommended by the Working Party on the co-ordination of policies regarding credit insurance, guarantees and financing credits. The Member States are to consult one another before guaranteeing private credits for a period longer than five years.

18 May
- Portugal applies for association with the EEC.

23 May
- Programme for the implementation of common transport policy.

25 June
- Inter-executive Working Party on energy transmits to the governments a memorandum on energy policy.

24 July – First Council directive on the establishment of common rules for certain international road transport operations for hire or reward.

30 July – Entry into force of the first regulations establishing a common organization of markets in cereals, pigmeat, eggs, poultrymeat, wine, and fruit and vegetables.

July-August – First recommendation in the social field: European list of occupational diseases, industrial medecine, social services for workers moving within the Community.

25 September – Programme for the implementation of commercial policy adopted by the Council.

11 October – The US President signs the Trade Expansion Act.

1 November – Programme for the second stage of the transition period submitted by the Commission, which again proposes more rapid development of the common market.

5 November – First draft directive to harmonize turnover taxes in three stages submitted by the Commission to the Council.

4 December – Council decision on the co-ordination of agricultural structure policies (establishment under the aegis of the Commission of a Standing Committee on Agricultural Structures).

10–15 December – European conference on social security in Brussels.

18 December – Adoption by the Council of a second directive supplementing and amending the first directive for the implementation of Article 67.

20 December – Initialling of the new EEC-AASM Association Agreement.

1963

The opening of the year saw the failure of negotiations between Great Britain and the Community. The implementation of the Treaty continued; a further 10% reduction in tariff duties was applied in July, as well as the second alignment of national tariffs towards the common customs tariff. For industrial products, the Community was two and a half years ahead of the schedule set by the Treaty.

The Council, on the Commission's proposal, established the general principles for a common vocational training policy. A programme for social harmonization (labour, social security, etc.) was also prepared by agreement with the governments of the Member States. Further common market organizations were decided. They were to apply to milk and milk products, beef and veal, and rice.

The Commission submitted to the Council its first proposals for a programme to establish a common transport system and a new convention of association for five years with the overseas associates was signed at Yaoundé in July.

An association agreement with Turkey was signed in September and a trade agreement with Iran in October.

The EDF financed 43 development projects to a total of 45 million u.a.

29 January – Negotiations on Great Britain's entry into the Community adjourned sine die.

1 February – One year after the entry into force of Regulation No. 17, the Commis-

sion has already received some 34 500 notifications, 30 000 of which concern exclusive dealing agreements.

5 February – The Court of Justice for the first time recognizes that the Treaty contains provisions producing immediate effects conferring rights on individuals (Case 26/62, known as "Tarief-Commissie").

21 February – Council regulation on the social security of frontier workers.

2 April – The Council adopts the general principles of a common vocational training policy.

16-21 May – Ministerial meeting in Geneva: first decisions of principle on the opening of the Kennedy round.

1 July – Algeria requests the opening of talks with the EEC.

11 July – Regulation on the social security of seasonal workers.

20 July – Signing at Yaoundé of the Association Convention between the Community and 18 African States including Madagascar.

10 September – Nigeria requests the opening of negotiations with the EEC.

12 September – Association Agreement with Turkey signed at Ankara.

14 September – The Commission adopts its programme concerned with social policy in agriculture.

23-24 September – Agreement in principle by the Councils on a merger of the Executives.

24 September – Tanzania, Kenya and Uganda request the opening of negotiations.

14 October – Trade agreement signed between the EEC and Iran.

18 October – Tunisia requests the opening of negotiations with the EEC.

5 November – The Commission submits proposals for fixing common cereal prices in a single stage and a Community plan for the Kennedy negotiations.

14 December – Morocco requests the opening of negotiations with the EEC.

23 December – The Council decides the mandate given to the Commission for the Kennedy negotiations.

– Council agreement on the basic regulations concerning rice, beef and veal, and milk and milk products.

1964

This year the Community moved more definitely towards a concerted economic policy. Already in April, the Council of Ministers strengthened the co-operation of member countries in monetary and financial policy, setting up a Committee of Governors of Central Banks and a Budget Policy Committee, at the same time widening the powers of the Monetary Committee. It decided on the planning and execution of a medium-term economic policy for the Community, including the establishment of a Medium-term Economic Policy Committee. It sent a first recommendation to the six countries for concerted action in short-term economic policy.

In May, the second regulation on the free movement of workers within the Community came into force.

The year was also marked by the beginning of the greatest commercial negotiation ever to take place, known as the Kennedy round. The negotiations were to apply to all classes of products (industrial and agricultural, primary and manufactured) and were to concern not only tariff duties (working hypo-

thesis: 50% reduction) but also non-tariff obstacles. The talks began on 4 May in Geneva.

In October, the Commission sent to the Council and to the governments of the Member States a memorandum entitled 'Initiative 64". The Commission proposed to advance the date for the attainment of customs union, to promote harmonization of customs legislations, and to remove fiscal and semi-tariff obstacles in intra-Community trade.

The common agricultural market progressed. The milk, milk products, beef and veal, and rice regulations came into force. The common agricultural policy was to apply to approximately 85% of agricultural production by 1 November 1964. Community financing of agricultural expenditure—market support, refunds on exports and the agricultural guidance sector—was applied progressively. In December, the Six adopted the plan for unification of cereal prices; common prices were to be applied from July 1967 onwards.

In June, a trade agreement was signed with Israel. The association of the Netherlands Antilles with the Community took effect in October.

The second EDF began its activities and financed 15 projects to a total of 24 million u.a., while the first EDF financed a further 28 projects representing 32 million u.a.

5 February
- Adoption of regulations on milk, milk products, beef and veal, and rice, and of two regulations on the financing of the common agricultural policy.
- Opening of exploratory talks between the EEC and Tanzania, Uganda and Kenya.
- Council decision on the association of the Overseas Countries and Territories with the EEC.
- Opening of talks between the EEC and Algeria.

11 March
- The Commission decides its first case concerning restrictive practices.

23 March
- Geneva: opening of United Nations Conference on Trade and Development (UNCTAD).

March
- A preliminary draft convention for the creation of European patent law transmitted to the governments of the Member States.

15 April
- Adoption by the Council of important decisions on the development of Community economic policy, including the setting up of a Medium-term Economic Policy Committee.

21 April
Adoption by the ECSC Special Council of Ministers of a protocol of agreement on energy policy, covering coal, hydrocarbons and atomic energy.

1 May
- Entry into force of second regulation on the free movement of workers.

4 May
- Official opening of GATT negotiations (Kennedy round).

8 May
- Adoption by the Council of the CCT for petroleum products, last of the List G products (to apply from 1 November 1964).

1 June
- New Convention of Association with the overseas countries comes into force.
- Council adopts financial regulations of the EDF.

4 June – Trade agreement signed with Israel.

12 June – Submission by the Commission to the Council of amended proposal for the directive on the harmonization of turnover taxes.

8 July – First meeting of EEC-AASM Association Council in Brussels.

15 July – By its decision known as Costa/Enel (Case 6/64), the Court of Justice recognizes the primacy of Community law over national law in the event of conflict.

1 September – Rice regulation comes into force.

23 September – The Commission makes a decision on cartels in the leading case of Grundig-Consten.

30 September – Proposal of the Commission in "Initiative 64" for a new acceleration of the common market for 1 January 1965.

1 October – Association of the Netherlands Antilles with the Community.

1 November – Regulations on beef and veal and on milk and milk products come into force.

15 November – Adoption by the Council of the lists of exceptions for industrial products proposed by the EEC in the Kennedy negotiations.

15 December – Council decisions on the common level of cereal prices from 1 July 1967.

1965

The dominant feature of the year was what is commonly called the "crisis of 30 June". The Council did not agree to a set of Commission proposals, connected with the financing of the common agricultural policy, that the creation of the Community's own financial resources and some limited institutional progress should accompany the achievement of customs union. In April, the Six signed the Treaty setting up a single Council and a single Commission of the European Communities. In June, the Council reached agreement on the common organization of the market in goods transport by road, rail and inland waterway.

The dismantling of internal tariffs continued. On 1 January, intra-Community duties on industrial products were reduced to 30% of the original duty. The remaining duties on agricultural products were at 50% or 45% of the original duty depening on the product.

March saw the opening of negotiations with Austria. In May a trade and technical co-operation agreement was signed with the Lebanon.

The second EDF financed 88 development programmes and projects to a total of 183 million u.a.

1 January – A further 10% reduction of customs duties, bringing the rates down to 30% of their 1957 level.

2 March – Commission empowered by the Council to exempt, by way of regulation, whole classes of agreement from the Treaty ban on cartels.

9 March – The Council passes a regulation on the institution of a Community quota and on the adaptation of bilateral quotas for road haulage between the Member States, the entry into force of which is subject to an agreement on organization of the transport market.

19 March – Opening of EEC negotiations with Austria.

31 March – Submission to the Council of the Commission's proposals for the financing of the common agricultural policy.

8 April – Signing of the Treaty merging the three Executives.

11 May – The Commission adopts and communicates to the Council a programme for the implementation of a common policy on vocational training in agriculture.
– First communication of the Commission to the Council of the Community's regional policy.

13 May – The Council adopts a decision on the harmonization of arrangements affecting competition in rail, road and inland water transport.

21 May – Signing of the agreement on trade and technical co-operation with the Lebanon.

15 June – The Council adopts a regulation creating a system of agricultural accounting information.

22 June – Agreement in the Council on rates to be instituted under the common transport policy and on the operating conditions of the market.

30 June – Disagreement in the Council on the financing of the common agricultural policy. The French Permanent Representative is recalled to Paris.

7 July – Commission recommendation on the housing of workers and their families moving within the Community.

22 July – Commission memorandum to the Council on the financing of the common agricultural policy and on the Community's independent resources.

26–27 July – First Council meeting in the absence of France.

26 October – The German, Belgian, Italian, Luxembourg and Dutch governments, meeting in the Council, solemnly reaffirm the necessity of pursuing the fulfilment of the Treaties of Rome and Paris.

20 December – Five-man Council in Brussels. Preparation for resumption of talks with France decided for mid-January.

23 December – The Commission submits to the Council a memorandum on industrial concentration in the Common Market.

1966

The political crisis was resolved in January at Luxembourg, where the Council of Ministers met in extraordinary session. Though there was no unanimous agreement on the adoption of decisions by majority vote, the Ministers decided that the fact of this disagreement need not be an obstacle to the continuation of Community activity.

In May, the Council overcame the obstacle which it had met with in June 1965. It adopted general decisions on the financing of the common agricultural policy. A timetable was drawn up for the achievement of free movement of agricultural and industrial goods for 1 July 1968. The Council moreover stated the objectives which it was setting itself in commercial policy, harmonization of taxes, social policy and regional policy. The GATT negotiations continued with renewed impetus.

In July, the Council decided to create common market organizations in fruit and vegetables, sugar, and oils and fats. It determind common prices for milk products, beef

and veal, rice, sugar and vegetable oils.
In October the Council adopted a resolution on means of overcoming the difficulties arising in transport policy.
Further progress was made on the road to economic union: the first mediumterm economic programme for 1966–70 was drawn up and submitted to the Council. The Commission sent the Council a memorandum on the creation of "European-incorporated" companies. An association agreement was signed with Nigeria.
The second EDF financed 62 development programmes and projects in connection with the Yaoundé Association to a total of 131 million u.a.

1 January – Eighth reduction of intra-Community customs duties, bringing them down to 20% of the original duties for industrial products and 35-40% for agricultural products depending on the product.

17-18 January – Luxembourg: steps towards a solution of the crisis. Extraordinary meeting of the Council in Luxembourg at which France is present for the first time since July 1965.

28-29 January – The extraordinary Council of the Six meeting in Luxembourg agrees to resume normal Community activity.

16 February – First Commission memorandum to the Council on a common policy for oil and natural gas.

4 March – Commission proposals on common prices for milk and milk products, beef and veal, sugar, rice, oilseeds and olive oil.

25 March – The Commission submits to the Council a report on aids to agriculture and a proposal on rules of competition in agriculture.

22 April – The Commission submits to the Council a memorandum on the creation of "European-incorporated" companies.

11 May – Decision in principle on the financing of the common agricultural policy up to the end of the transition period and on a timetable for the establishment of free movement of agricultural products by 1 July 1968.

13 July – Judgment of the Court of Justice in the Grundig-Consten case (56 and 58/64) confirms the Commission's view that cartels of the type known as vertical are not outside the scope of Article 85 of the Treaty.

16 July – Association agreement between the Community and Nigeria signed in Lagos.

28 July – The Council adopts a regulation concerning the introduction of common rules for international road passenger transport.

4 October – Israel applies for association with the Community.

10 November – Olive oil is the first agricultural product to reach the single market stage. Common prices come into force.

25 November – The Commission transmits to the Council a report on the situation of the fishing industry and on the basic principles for a common policy in this sector.

23 December – Proposals by the Commission to the Council for regulations concerning cereals, pigmeat and sugar at the single market stage.

The Community is preparing to round the cape of 1 July 1968, the date when customs union and the common agricultural policy must be fully established.

The Commission is applying itself to removing all obstacles to the free movement of goods. Work is in progress for the harmonization of customs legislations, and the removal of semi-tariff obstacles and frontier controls.

In fiscal matters, an important step forward was made when the Council adopted in principle the structure and manner of application of a common value added tax system.

With regard to transport, the Commission is drawing up measures to accelarate implementation of the common transport policy following the Council resolution of 20 October 1966.

At a time when the European Economic Community is celebrating its 10th anniversary, the process leading to economic union, a near neighbour of customs union, is going forward steadily. In this context, the adoption in February of the first medium-term economic programme (1966-70) by the EEC Council of Ministers and the governments of the Member States is of special importance.

By 23 March 1967, the first and second EDF had financed since their inception 561 development programmes or projects to a total of 962 million u.a. for the benefit of overseas countries and states associated with the Community.

January
- The Commission lays down the broad lines for its work on social matters.
- Commission recommendation to the Member States on the protection of young workers.
- Memorandum from the Commission to the Council on common transport policy following the Council resolution of 20 October 1966.

18 January
- Commission proposal to the Council on the single market stage for eggs and poultrymeat.

8 February
- The Council and the governments of the Member States adopt the first medium-term economic programme.
- The Commission submits to the Council an amended proposal for the third directive for the implementation of Article 67 of the Treaty.

9 February
- The Council adopts the two directives proposed by the Commission concerning the harmonization of turnover tax systems.

21 February
- The Commission submits a draft regulation to the Council concerning agricultural producer groups and unions thereof.

23 February
- The Commission submits to the Council a draft regulation establishing a common market organization for plants, flowers, bulbs, etc.

2 March
- The Council approves the regulation on social security for seamen.

14 March
- The Commission agrees to issue a regulation concerning the application of Article 85(3) to classes of exclusive agreement. This regulation will enable cases of exclusive dealing agreements to be settled en blow.

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SUPPLEMENT to this issue (Supplement D)
Body of Laws on Direct Taxation in the Somalian Republic

THIS BULLETIN ISSUE
is devoted to tax rules in India and Indonesia; the Supplement contains the text of the new codified laws on direct taxation in the Somalian Republic. To complete Mr. Jaitly's article on the Tax Liability of Foreigners on Business Transactions in India the text of the new Agreement between India and Greece has been inserted. In order to provide a basis for comparison the Agreement for Double Taxation Relief between India and Aden has been given.

Besides these contributions, which are on an informative practical basis, Mr. Halpern of Austria describes the reasons behind the Austrian Development Act 1966 and Mr. Pepper considers the Taxation of Wealth all over the world from a theoretical and practical point of view.

CE NUMERO DU BULLETIN
est consacré aux règles fiscales en Inde et en Indonésie; le Supplement contient le texte des nouvelles lois codifiées de la législation fiscale directe au République des Somalies. Afin de compléter l'article de Monsieur Jaitly sur les obligations fiscales des étrangers quant aux transactions commerciales en Inde nous avons inseré le texte du nouvel accord conclu entre l'Inde et le Grèce. De plus pour permettre une base de comparaison nous avons ajouté les mesures d'allégement a la double taxation, intervenus entre l'Inde et Aden.

Outre ces articles qui ont un caractère d'ordre pratique, Monsieur Halpern d'Autriche décrit les raisons qui se cachent derrière la loi de Développement Autrichien 1966, tandis que Monsieur Pepper présente de vue théorique et pratique l'imposition de la richesse à travers le monde.

DIESES HEFT DES BULLETINS
behandelt die Steuerregeln in Indien und Indonesien. Das Supplement befasst den Text der neuen kodifizierten Gesetzgebung über die direkten Steuern in der Republik Somalia. Als Ergänzung zum Artikel von Herrn Jaitly über die Steuerpflicht von Ausländern, die geschäftliche Transaktionen in Indien ausführen, ist der Text des neuen Doppelbesteuerungsabkommens zwischen Indien und Griechenland aufgenommen, sowie um einen Vergleich ziehen zu können, die Massnahmen zur Vermeiding der Doppelbesteuerung zwischen Indien und Aden.

Neben obengenannten Beiträgen die von positiv-rechtlicher Art sind, beschreibt Herr Halpern welche Motive den österreichischen Wachstumsgesetze 1966 zu grund gelegen haben. Herr Pepper widmet eine eingehende Betrachtung der Vermögensteuererhebung, vom theoretischen und praktischen Standpunkt aus gesehen.

* * * * ARTICLES * * * *

H.W.T. PEPPER:

THE TAXATION OF WEALTH

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INTRODUCTION

ARGUMENTS IN FAVOUR OF WEALTH TAX

Wealth tax, otherwise known as capital tax, or net worth tax, is usually understood to be an annual tax on wealth which is normally to be paid out of the annual product of the wealth in question (see paragraphs 15-26).

2. Where a wealth tax is intended to be such as could only be met out of the realisation or partial realisation or of the wealth or capital, it is more properly described as a capital levy and will be so treated in these notes.

3. Wealth taxes exist in a number of countries (see Appendix) and have been advocated as a means of raising revenue which has less disincentive effect than direct taxes on income. A reference to the possible use of a wealth tax in this sense was recently made, for example, in the British Report on "Conditions Favourable to Faster Growth".[1])

4. Other reasons[2]) advanced as favouring the introduction of wealth tax to replace taxes at the higher rates on income include the following:

(a) a tax at common rates on all types of capital favours capital which is employed the most productively and penalises capital which is idle or under-employed;

(b) when capital assets appreciate, a wealth tax would tax them at their higher value whereas income tax would not tax such an appreciation unless it gave rise to a corresponding increase in income;

(c) there is less opportunity for the shifting of capital taxes on to consumers compared with taxes on profits or incomes; and

(d) income from wealth is more secure than income from labour and where income tax is levied equally on both types of income there is a case for an additional tax on the former.

TAXABLE CAPACITY OF CAPITAL

5. A major premiss in the argument for taxing capital and one which is often quoted is that "the ownership of property in the form of disposable assets endows the property-owner with a taxable capacity as such . . ."[3]) This statement is really an argument for taxing capital by means of a capital levy because this is the only tax which capital, per se, is able to "bear", assuming that the income from the capital is charged to income tax, and gains from capital realisations are charged to capital gains tax.

ARGUMENTS AGAINST WEALTH TAX

6. Some of the arguments against wealth tax are as follows:—

(a) some unproductive capital is merely temporarily so—for example equity capital invested in an enterprise which is a new high risk venture may not see much return on capital for a few years. There are also investments which are low yielding for a contrary reason—because the industry is depressed or inefficient. A wealth tax would bear harder on the first-mentioned types of venture because of its probably greater market (and taxable) value. But the newer and therefore riskier venture is the very type of investment the wealth tax is intended to favour;

(b) a person (A) who had say, £100,000 invested in gilt-edged at 6% and a person (B) with a life annuity or pension of £6,000 have

---

1) National Economic Development Council, 1963, page 42 (H.M.S.O.);

2) Although there would seem to be a theoretical case for wealth tax as a partial or full substitute for death duties, it does not seem to be advocated for such a purpose in current controversy.

3) Professor N. Kaldor "Indian Tax Reform" Page 20.

the same income. B has no capital but has an equal assurance that his income will last his lifetime. A has greater capacity to pay only by realising his capital and hence reducing his future income;

(c) where undated gilt-edged investments were bought at a time when the going interest rate was 3% and the rate has since advanced to 6% or 7% the investor, who may be a rentier or the trustee for a widow or orphans, is getting a poor return for the money invested. The investment may however have been made on the grounds of patriotism or for security of money income. There are a great many such holders of gilt-edged securities and it would seem inequitable in such cases that the holder's interest should in effect be subject to heavier additional tax (because of the low yield) on original capital than income from a business which produces a higher yield;

(d) the incidence of wealth tax is likely to be unequal in respect of a large proportion of non-monetary assets, for example, (i) business goodwill in the respective cases where this has been

(A) purchased, or

(B) built up by the efforts of the present owner,

(ii) property which is subject only to infrequent re-valuation, or (iii) a mining or plantation venture which will take some years to come to the income-producing stage but meantime represents considerable "disposable" wealth. Some of these types of assets will be examined in more detail below. In some instances the problems which would occur for wealth tax would not arise for income tax, in other cases similar problems occur in both taxes;

(e) the "pro" argument that wealth taxes are less likely to be shifted on to consumers is not tenable where the wealth is the business assets of a business man, especially where the tax is charged along with his income tax as is sometimes advocated. The businessman is likely to regard the tax as another business overhead to be covered in his prices. Where the taxpayer is a private investor in equity shares the tax certainly cannot be shifted but then the investor is himself a consumer. The tax moreover is intended to encourage investment in more productive activities and it is not clear what more the taxpayer whose total capital is in equity shares is expected to do. His wealth tax however will be the same as that of another investor who has his capital in fixed interest securities;

(f) to the extent that capital values accord with income-bearing propensity, wealth tax has no demonstrable advantage over income tax. Where capital values and income potential diverge, a wealth tax is just as likely to be capricious as it is to be logical in its incidence;

(g) although the case for some differentiation in taxation between income from investments and from labour is sound the differentiation can more readily be made within the income tax framework. Either a special deduction could be made in assessing the latter to tax or a surcharge could be levied on the tax charged on the former.

INCIDENCE OF WEALTH TAX:

: GOODWILL

7. If individuals' shareholdings are included in their taxable wealth and companies exempted (to avoid double taxing the wealth represented by the shares) the value of the company's goodwill is reflected in stock market prices and would thus be within the scope of wealth tax. In the case of a business

run by an individual however who has developed his own goodwill (and not bought it ready-made) it is not usual to include the value of goodwill in the business capital for wealth tax purposes. If goodwill were to be included in such cases the valuation problem would be immense but exclusion gives the businessman a tax advantage over the equity investor. Both the business man and the equity investor however have their part to play in the development of a country and a tax that discriminates between them, other than for some purely short-term objective, is difficult to justify.

8. Even the discrimination between one business-man and another on the basis of whether he has built up his goodwill or bought it ready-made may prove anomalous. For example, assume that A has built up his own business and then sells it in order to buy the larger business built up by B who wants to retire. Although A has merely switched his investment his wealth tax will now be materially larger (although the transaction does not alter the quantum of his wealth) because of the inclusion of the "bought" goodwill is the new computation and the exclusion of goodwill from the previous computation.

PROPERTY

9. The valuation of real-estate is always a difficult operation as the litigation on compensation terms when property is compulsorily acquired clearly indicates. In practice valuations made for other purposes are often adopted for wealth tax. Such valuations may be out of date, and accordingly too low but are not likely to be objected to on that account by taxpayers.

10. Where valuations for local taxation purposes are adopted for national wealth tax purposes there may be an "incentive" to the local authorities to perpetuate old, out of date, valuations where it is felt that to increase them would merely enable the central government to collect more wealth tax as central revenue. Where the rate of local taxation can be freely varied, the use of old valuation figures is not necessarily a handicap in the collection of local revenue so long as the valuations of different properties are roughly in proportion to each other.

11. An anomaly will of course arise concerning wealth tax in these circumstances because wealth invested in such property will be taxed more favourably than wealth invested in other ways. On the other hand because real property is more readily identified than other assets the owner is more likely to be taxed fully.[4])

NEW INDUSTRIAL VENTURES

12. Assets which often represent a good deal of the wealth of developing countries are those included in mining and plantation industries where it may be some years before any yield can be expected from large capital outlays in new enterprises (in the case of a rubber plantation, up to seven years). No income tax is chargeable in the absence of profits but if this criterion is also used for the purposes of a wealth tax exemption this makes the latter even more difficult to justify as a distinct levy. If exemption is not made the tax is more logical as one covering all types of wealth but there is even less logic in the claim that it favours risk-bearing enterprise.

CONTRAST BETWEEN WEALTH TAX AND CAPITAL LEVY

13. Protagnonists of wealth taxation, while referring to the alleged innate capacity of wealth to bear tax, also refer to the fact that

4) This was the reason given for the abolition, after three years, of the wealth tax in Japan, i.e. that it was inequitable in that it was levied more efficiently on owners of real property than on owners of other types of wealth.

wealth taxes are actually in operation in a number of countries in different parts of the world. It is reasonably clear however that in the practical application of wealth taxes (see paragraphs 15-26) the intention of the legislators is that the tax bill should be paid out of income, not out of capital. There are minor exceptions to this principle which will be referred to below (paragraphs 33-35). The case for a capital levy, which is a different levy from wealth tax as actually practised, is also considered separately below (paragraphs 83-113).

CONSIDERATION OF TAX BASE

14. One comment will suffice for the moment on the respective merits of wealth taxes which fall respectively on income and capital. Fiscal policy is normaly directed to stimulating economic activity so as to widen and expand the taxable base. When such policy is successful in encouraging the growth of profitability, the yield of direct taxes based on profits is automatically expanded. By encouraging the growth of production and productivity it may be expected that taxes on production and consumption will yield an expanding revenue. On the other hand a tax on capital as such, by inevitably reducing the capital on which it falls, reduces the taxable base for the next such levy. A tax which erodes its own base will, other things remaining equal, obviously have only a limited future in the fiscal scene.

WEALTH TAX AS A TAX ON INCOME

15. Although, as noted above, one of the justifications quoted for wealth taxation is the (arguable) one that wealth has a taxable capacity per se, in practice, even in countries which regard the tax as a "socialist" measure, the tax burden falls upon income rather than on capital.[5])

16. It is significant that wealth tax is usually advocated as means of reducing income and surtaxes, that is, it is to be a partial substitute for, not an addition to the full pattern of existing direct taxes.

17. For example, the Shoup Commission recommended wealth tax in Japan concurrent with a reduction of the higher rates of personal income tax. The recommendations were adopted in 1950 when wealth tax was introduced at rates of from 0.5% to 3%, while the top income tax rate was reduced from 85% to 45%.

18. Several countries incorporate "ceilings", limiting the impact of their wealth tax, such as are likely to ensure that the levy may be paid out of income without impinging on capital. For example in Norway a ceiling of 85% of total income operates to limit the impact of income tax and wealth tax combined. The combined charge of the two taxes must not exceed the ceiling set. In Sweden a similar ceiling to the impact of income tax and wealth tax is provided—in this case the ceiling is 80% of total income.

19. In Pakistan there is a ceiling of 15% of income which however applies to the impact of wealth tax alone, not to the combined total of income tax and wealth tax.

20. In Ceylon, Wealth Tax was advocated by Professor N. Kaldor as one of the fiscal measures "suited to the needs of a democratic socialist community".[6]) The tax was adopted by the Government initially on the basis of a rate scale of ½% to 2% as recommended by Professor Kaldor but subsequently the rates were raised to a scale of 1% to 5%. The explanation given by the Finance

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5) The exception is the application of a selective wealth tax to undeveloped property discussed in paragraphs 33-36.

6) N. Kaldor. "Suggestions for a Comprehensive Reform of Direct Taxation". Sessional Paper IV 1960. Ceylon.

Minister, the Hon. U.B. Wanninayake, M.P. when announcing reduction of rates in the Budget Speech on 9th August, 1965 is indicative of the fact that, at least at the practical level, wealth taxation is to be regarded as a charge on income.

21. The Minister pointed out that the maximum rate of 5%, which applied to the Ceylon Wealth Tax for 1964/65, was equivalent to an income tax of 50% if the wealth yielded an income of 10%. This with income tax at the top rate of 80% meant total taxation of 130%. If the wealth yielded less than 10% income the effective tax rate would be considerably higher.

22. The Minister went on to say:

"This is not the concept underlying the Wealth Tax. Wealth Tax provides for a measure of differentiation in the burden of tax between earned and unearned income. It is in effect an additional Income Tax payable out of income."

He announced reduction of the rates of wealth tax to a scale ½% to 2%, the 2% applying on the excess of wealth over Rs. 1.8 million while the income tax rates were modified by substantial abatements which were to be allowed to taxpayers who made savings in certain forms.

23. Further evidence of the practical link of wealth taxes with the income from that wealth, which supports the definition of wealth tax as in effect an additional income tax payable out of income, is the provision in the Danish wealth tax which abates the tax payable where the yield from the capital is less than 3%. In Denmark, however, it is possible for the wealth tax to impinge on capital. The rebate where total taxable income is below 3% of capital amounts to 5% for every 0.2% that the income falls short of 3%. If the income is NIL therefore the rebate is 75% but there is still some tax payable out of capital in the absence of any income. If there is negative income i.e. a loss, the rebate is 80% which still leaves tax of up to 0.40% of the capital, (if it exceeds kr. 1,000,000), payable.

24. One of the most recently introduced wealth taxes, the Patrimony Tax levied in Chile is based on capital but the capital is converted to "income" at the fixed rate of 8%, the presumed income then being taxed at graduated rates which are equivalent to wealth tax on a scale from 0.6% to 2.8%. The tax is being levied for a 3-year period 1965-1967, and is further linked with income by the fact that a deduction from the patrimony tax may be made of one-half of the complementary income tax levied on total income.

EXEMPTIONS FROM WEALTH TAX

25. Exemptions from wealth tax allowed in various other countries include such items as copyrights, and patents held by authors and inventors respectively, furniture, life assurance policies, agricultural land, residences, animals, including racehouses, jewellery, money in current bank accounts. Some of these items are non-income bearing and others are of the type commonly afforded preferential tax treatment sometimes more to avoid administrative problems than as a matter of principle.

26. The effect of excluding various selected assets from the scope of wealth tax is to apply the tax unevenly between different taxpayers who have the same total wealth but who have it invested in different forms.

WEALTH TAX IN PRACTICE

27. As already noted wealth taxes are widespread, appearing in form or another in all the continents except Australia.

TAXATION BY REFERENCE TO INDICIA OF WEALTH

28. Apart from the more formal wealth taxes an element of wealth tax is implicit in the French system of assessing income tax liability partly by reference to external indicia of wealth which is also used in countries as far apart as Indonesia and Latin America. The wealth tax "principle" referred to above in paragraph 5 i.e. that wealth itself has a taxable capacity, is sometimes developed into the notion (justifying the tax as an economic "prod") that if the wealth is not producing commensurable taxable capacity (in the shape of income or capital gains) it ought to be employed so that it does.

29. To tax by reference to external indicia of wealth rather than by strict reference to ascertained income or gains is thus a limited form of wealth tax, limited because many, probably most, types of wealth neither have external indicia nor are readily visible to an outdoor tax assessor and these types thus escape such methods of taxation[7]).

HISTORICAL APPLICATIONS

30. The "external" test was used by Henry VII's Chancellor, Morton in Britain at a time when taxation policies were crude and rudimentary but his exactions fortunately were not perpetuated in the revenue system. In other ages however taxes were certainly levied at specified rates, on specific luxuries of the rich and middle classes but that is a different matter. (See also paras. 48-58)

PROPERTY TAXES

31. Many countries without formal wealth taxation levy this kind of tax, in effect, on certain forms of wealth. Land and real property are the most popular choices and in examining such taxes a distinction has to be drawn between the true wealth tax on the total property of a wealthy man and other property taxes which are levied to finance local services and government and of which the real impact is on the tenant.

32. A good deal of local taxation is raised from annual taxes on property levied usually by reference to the annual or rental value, or the capital value of the property. The tendency is for the tax to be levied on the occupier or, if charged on the landlord, to be passed on to the occupier and where the tax is to cover services such as roads, street lighting, sewerage, water, schools, libraries, etc., which directly benefit the occupier and his family, there is every reason why the occupier should pay. In these circumstances however the tax is demonstrably not one upon the wealth of the landlord. Since the property is not owned by the tenant the tax can hardly be regarded as upon his wealth in any direct sense and yet, since his contribution to the cost of local services is, in effect, being measured by the style in which he lives (i.e. the value of his residence), there is after all an "indicia of wealth" element in the tax.

VACANT LAND

33. One form of property tax which has been used over a long period in a number of different countries is the tax on empty land

7) The famous "Morton's Work" whereby those with external indicia of wealth were presumed to have equivalent capacity to pay and those without such indicia were presumed to have available the money which might otherwise have been spent on such paraphernalia.

with development value or undeveloped sites in cities. A recent example is the tax on undeveloped land introduced in Guyana in the Budget of 17th January, 1967. There is usually a twofold economic justification for such taxes which inescapably fall on the owner since there is no tenant.

34. Where economic development is being held up by the attitude of the owners of land in key positions who demand a high price for their land, and are prepared to wait a long time to obtain it, a tax on unused land may be a better device than requisitioning, with compensation, to encourage more rapid development. The tax has been reasonably successful in this respect in a number of countries. Where a valuable site in a city is left undeveloped the local authority may well consider it is being unreasonably deprived of potential tax revenue and include such property in the scope of its tax accordingly.

35. Where the local taxation system already charges tax at a low percentage on capital value rather than at a higher rate on rental value there will of course be no particular administrative difficulty in applying the tax to vacant lots.

36. Although this particular application of property tax is to land which has no real taxable capacity there is the justification outlined above which outweighs other considerations. The taxable capacity will be created when the owner either sells the land, realising a capital gain, or develops it himself to secure income.

SELECTIVE AND QUASI-WEALTH TAXES

SELECTIVE TAXES

37. Reference has already been made to taxes which apply only to particular types of assets or manifestations of wealth, e.g. huts, houses, or cattle. In some cases wealth tax itself is limited in scope, e.g. that in Indonesia which applies basically to immovable assets.

38. Taiwan's "Household Tax" applies to real estate owned by individuals and business corporations and extends also to plant and machinery, but not to that used in agricultural production. This local tax, though selective, is reasonably productive and yields over 3% of total national revenue (1964 figures). Land and real estate in general are in fact the assets most commonly selected for wealth taxes which do not extend to total wealth.

39. Stamp duties are sometimes used to levy charges which are tantamount to a tax on wealth, e.g. to those on the authorised and/or issued capital of limited companies, or on the acquisition of real estate.

QUASI-TAXATION

40. Apart from land and property taxes charged annually upon the capital value of such assets, it may be noted that rent restrictions which are imposed in some countries to freeze or limit the rents payable on property, particularly property occupied by the lower-income groups, represent a form of wealth tax on property, the capital value of which is reduced by the restriction on its earning capacity.

41. A similar result is produced by other types of restriction, for example, compulsory dividend-limitation during a deflationary period which reduces share prices or keeps them at a lower level than would operate without the limitation.

42. Taxpayers who are forced to sell property or shares during a period of compulsory rent or dividend restriction are being "taxed" as effectively as if a general wealth tax were being applied to their assets except

that there is no revenue yield. The impact is however selective, uneven, and inequitable and hence such measures are, or should be, only of temporary duration.

43. During the period of restriction the taxpayers concerned are, in effect, subjected to an additional income tax to the extent to which the income limit falls short of the "natural" level which would operate in the absence of restrictions. This type of "tax" also operates unevenly because the difference between the restricted level and the "natural" level of income will vary considerably from one property or shareholding to another.

44. Unless it is part of deliberate economic policy to encourage the investment of capital in channels other than those which are the subject of income-restriction it is clear that such restrictions should be imposed for as brief a period as possible. This is in fact usually the case with dividend limitation[8]) but as regards rents the restrictions usually have strong political connotations and once imposed are not easy to remove without a degree of political bravery. While restrictions continue they are self-defeating to a degree because they discourage the investment of capital to provide more housing[9]) and thus defer the attainment of equilibrium in the property market which might make restrictions unnecessary.

EVOLUTION OF SELECTIVE WEALTH TAXES

45. In general the tendency is for selective wealth taxes to evolve into more general taxes. The simplest form, a hut or house tax gives an incentive to avoidance by persons crowding into a single establishment and thus evolves into a poll tax on individuals (see paragraph 54). A poll tax soon has to take account of personal circumstances and thus becomes a graduated poll tax and eventually perhaps an income tax. Evolution may however take place in a different direction — from a fixed tax on a dwelling to a levy which is graduated according to the annual (rental) value, or capital value, of the dwelling and thus into a system of local rating or a property tax (see paragraphs 31-36).

46. Other, fairly crude forms of wealth tax, e.g. those on "external indicia" of wealth such as the numbers of windows, or of chimneys in a house, the number of servants kept, the use of armorial bearings (or family crests) on a residence or on carriages, usually become less financially significant as time goes on, are abolished as not worth collection costs and superseded by land or property taxes which bear a closer relationship to the value of the property although not to total wealth.

47. The logic of property taxation is however greater where the tax forms local revenue designed to defray the cost of local services since the cost will bear some relationship to the size of the dwelling. For example the cost of police protection and fire fighting services will be greater in coping with the greater risks of burglary and fire in the case of a large mansion than a single-roomed cottage. It is in fact often in the form of local revenue that selective wealth taxes survive. National taxes on the other hand are more usually based on total wealth or the income manifestation of that wealth.

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8) Note also that no great harm is done to a shareholder by short-term dividend limitation provided he is not forced to sell out during the limitation period because the "frustrated" dividends have not been lost but may be paid out as additional bonuses in subsequent years.

9) Note by way of contrast, the incentive to residential building provided by Hong Kong at the time of acute shortage because of a heavy influx of refugees. Rent income was charged at one-half the rate of tax on other income.

HISTORICAL AND RECENT APPLICATION OF WEALTH TAXES

48. Wealth taxes have a long history going back to ancient times when fractional levies on herds, flocks etc. were sometimes applied to the whole herd or flock (the "capital") and not to the year's net natural increase (the "income") so that the levies might, or might not, be payble out of income. The "jangali" or cattle head tax still survives in parts of Africa and India. The limitation of this ancient levy is that it covers only one kind of wealth (admittedly in circumstances where animals are the major criterion of wealth).

: BRITAIN

49. Britain in earlier times had a series of wealth taxes under various different titles and made substantial use of this form of tax. One of the main functions of the Domesday Book, compiled in 1086 as a register of all lands and property in England, was to serve as a basis for taxation. Real property was always an obvious target for taxation but in 1166 Henry II imposed an annual tax of 1d. per £ (approximately 0.4%) on moveable property, a type of tax which was continued at different rates and with certain exemptions (e.g. of food for personal consumption), throughout the period from the 13th to the 17th century. The tax, however, tended to be imposed intermittently, when the sovereign had urgent need of money.

50. In Edward I's reign assessments were made in the course of a house-to-house survey by local assessors and were checked by the country commissioners. On a number of occasions the tax was levied at a tenth or a fifteenth (10% or 6⅔rds%) and "fifteenth" remained the name for the tax even when the rates were reduced.

51. The tax levied in 1688 on moveables was significantly different in that it transmuted what was really a wealth tax into a tax on a deemed profit, i.e. 1/— in the £ (5%), the profit being deemed to accrue at 6% on the capital. The tax accordingly represented 6/— per £100 of the value (i.e. 0.3%) of goods, chattels, and personal property and was thus, alternatively, expressed. It is interesting to note that this mutation principle has recently been employed in the wealth tax (known as the patrimony tax and introduced in 1965 for three years' duration) currently operated in Chile. (See paragraphs 56 and 62.)

52. The rate of tax in this form was successively increased to 25/— per £100 (1.5%) and its last application was in 1714 at the rate of 12/— per £100 (0.6%) after which another form of wealth taxation, the land tax—which operated from 1692 to 1963—formed the main source of revenue from wealth, taxation. Land tax was charged at fixed rates on the annual value of lands whether producing a rent revenue or not but the ancient device of a fixed quota of revenue for each parish was incorporated so that the rate for a particular parish varied according to the ratio of the amount required to the total assesable annual value but could not be less than 1d., nor more than 1/—, in the £ (0.5%, 5%).

53. The raising of national revenue by taxing real property has now been completely taken over by income tax which still embodies (in Schedule B) a measure of wealth taxation in so far as it applies to the "value in use" of amenity lands which produce no tangible income to the owner, the capital gains tax which taxes realised increments of capital value, the estate duty which applies to assets transmitted by death, and the stamp duties on property transfers. Although local rating is a tax on property in proportion to its annual value it is basically a levy upon the occupiers to pay for local services

and is not usually payable, e.g. on house property which is unlet and unocuppied. Such local taxation does however contain a wealth tax element because the owner/occupier of a large mansion is taxed much more heavily in proportion to the service he receives than the occupier of a small cottage, the tax being related to the annual value of the residence occupied. This value is of course an important indication of wealth but unlikely to bear a fixed ratio to total wealth for a cross-section of occupiers.

: AFRICA

54. The early administrators in the less heveloped parts of Africa commonly used dut or house taxes to raise revenue. There was an element of graduation in that wealthier persons with several wives and several establishments paid more, than the monogamous. Occasionally a higher fixed rate was charged on large than on small houses. In general, however, such taxes gradually become levies on the occupants rather than on the dwelling (to prevent avoidance by any people crowding into one building) and then developed from fixed charges into graduated poll taxes and thence into a tax on income.

: GENERAL

55. In other parts of the world there appears to have been no common evolutionary process. Old wealth taxes survive in Austria, the Federal Republic of Germany, Holland, Luxembourg, Denmark, Norway and Sweden but in general do not produce a large revenue. In Ceylon, India, and Pakistan the tax has been introduced fairly recently, mainly as a result of the advocacy of Professor Kaldor. The yield in those countries is also relatively small compared to income tax, but there are no indications that the tax might be abandoned. Although the rates of tax in Ceylon were recently reduced, after a short-lived increase, the scope of the tax both in Ceylon and in India has in fact been widened in recent years by reducing the exemption limit and withdrawing exemption from certain types of assets.

56. In Indonesia the wealth tax applies mainly to immovable property and mortages theron but is charged only at ½%. Guatemala has recently doubled the rate of her wealth tax from 0.3% to 0.6% but Japan abandoned hers (the rates were from ½% to 3%), after a 3-year trial, in 1953. The country most recently to introduce a wealth tax is Chile (rates from 1.6% to 2.8%) but there the tax is declared to be for a short duration i.e. the 3 years 1965, 1966 and 1967. Other examples of wealth taxes currently in operation are to be found in the Appendix.

57. The present Chancellor of the Exchequer in Britain advocated introduction of a wealth tax during a speech made in 1963 but after assuming office in 1964 announced[10]) that he had no immediate plans for introducing such a levy.

58. For the reasons outlined in the paragraphs on the drawbacks of wealth tax (paragraphs 6-14) the administrative problems referred to in paragraphs 63-82, and the difficulty in demonstrating that the tax is generally superior to income tax (referred to in the paragraphs 15-26) it seems unlikely that wealth tax will sweep the fiscal world as income tax has done in the last quarter-century or so. Because, however, of the political overtones involved in the (at least

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10) In a written Parliamentary reply, Mr Callaghan announced (per London Times of 16th December, 1964)—
"In view of the major reforms I have already announced to modernise the tax system and make it more fair, I have no plans for proceeding with this proposal."

titular) taxation of wealth as such, and therefore of the "haves" rather than the "have-nots", and because in some countries wealth tax is a form of local revenue for which there is no obvious alternative, it is likely that wealth taxes of one kind or another will survive for some years to come.

DOUBLE TAXATION RELIEF FOR WEALTH TAXES

59. Bilateral treaties designed to avoid or abate double taxation where the taxpayer has income in one country and resides in the other are simplest to negotiate when the taxation systems of the two countries are broadly similar. Where each country has income and wealth taxes no problem arises as reciprocal relief can be given for both taxes (as, e.g., in the treaties between Ceylon, India and Pakistan, and Scandinavia).

60. In addition double tax treaties which deal solely with death duties are now becoming more common to provide relief where a taxpayer dies domiciled in one country and possessed of assets in the other.

61. Difficulty arises when one country has a wealth tax and the other has not because a country which has only income tax cannot give full credit for both income and wealth taxes imposed in the other. To some extent the difficulty may be met by one country granting exemption and allowing full taxing rights to the other but this is not possible for all types of income and the assets which produce it.

62. One type of wealth tax which appears to overcome the difficulty mentioned above is the temporary levy introduced in Chile (known as patrimony tax) for the years 1965, 1966 and 1967 which although based on capital (for the base year 1964) manifests itself as a tax on income at graduated rates. A taxpayer's capital is deemed to produce income at 8% per year and the deemed income is then charged, after a deduction of 1,300 escudos, at rates ranging from 20% to 35% (representing 1.6% to 2.8% on the capital) for each of the years 1965, 1966 and 1967. The income is computed by reference to the 1964 capital but the amount of tax payable is adjustable by reference to changes in the value of money in each tax year compared to the base year. Linking the tax more closely to income tax is the provision that one half of the amount paid as complementary tax (the income tax on total income) is deductible from the wealth tax due.

ADMINISTRATION

GENERAL

63. The administrative difficulties of wealth taxation if conceived as a "permanent" tax producing a sizeable revenue in an equitable manner are formidable. The greatest difficulty arises in deciding the precise tax base. The problems of valuation have already been alluded to but these are more fundamental problems reference to some of which—the treatment of annuities and pensions, of stocks and shares—and of gilt-edged securities—is made below.

ANNUITIES AND PENSIONS

64. A life annuity and a life pension are broadly similar in substance. Both are normally charged to income tax and do not represent capital that is disposable without reducing the income. Pensions are often non-assignable and therefore not disposable at all. It is hardly a practical matter to include the value of a pension (representing deferred

earnings of an employment) in taxable wealth. If pensions are excluded there is also a case for excluding annuities particularly where the latter's function is similar to that of a pension. If annuities are exempted from wealth tax this opens a field for tax avoidance to combat which involves some administrative complication.

TREATMENT OF STOCKS AND SHARES

65. It is usual, though not the invariable rule, to charge wealth tax on individuals and not on companies. If the tax is to be graduated (as is usually the case) this can only be achieved if an individual is taxed on his total wealth including the value of his stocks and shares. Excluding companies from wealth tax avoids double taxation of company capital. The practical method of valuing shares in public companies is to adopt the stock exchange quotation but this means that the company is valued by considerations (e.g. of dividend yield and future prospects) other than its capital as represented by its assets.

66. The principle that wealth tax should bear more heavily on wealth that is not profitably employed cannot operate if stock exchange valuations are used[11]) but since the investment by the shareholder is made at market price he can hardly be taxed on the basis of the underlying assets. As mentioned above, to tax the company instead of the shareholder would be more logical if the tax is seen as an economic device for encouraging high profitability but would alter the shape of the graduated tax burden on individuals.

GILT-EDGED SECURITIES

67. With gilt-edged securities also there is little choice but to adopt market value. The long term holder of low interest securities who has seen his investment fall in money value (because of rising interest rates) as well as in real terms, at least has the compensation of having only the lower money value included in his wealth assessment. To adopt any other basis, e.g. nominal value, would be neither fair nor feasible—the taxing Government must endeavour to make its public louns a marketable security and cannot in practice penalise purchase of them as an insufficiently enterprising investment.

APPRECIATION OF CAPITAL

68. The claim that wealth tax copes more rapidly with capital appreciation (see paragraph 4 (b)) may not be realised in practice as the burden of valuation is likely to be alleviated by using existing valuations made in earlier years for other purposes—see also paragraphs 75-86 below. Other valuation problems are also referred to in the following paragraphs.

VALUATION: GOODWILL : BUSINESSES AND PROFESSIONS

69. The inequality problem arising from the treatment of business goodwill was referred to briefly in paragraphs 7 and 8. The problem however also affects the comparative tax treatment of business and professional men. The price on business goodwill may attach more to the name of the business than to the personality of the proprietor. This is especially likely to the case of a large concern.

70. Goodwill is also a factor in professional earnings and hence in the capital value of the professional practice. In the case of a practising surgeon, lawyer or architect the good-

11) For example at the time of writing equity shares in the Cunard Shipping company can be bought for 12/6d. compared with an asset value of about 80/—.

will may by contrast attach itself to the person rather than to the practice. To the extent to which such goodwill is accordingly non-transferable it has no disposal value and therefore will not normally enter into wealth for tax purposes.

71. In the case of a profession nothing can normally be included in wealth for the value of the professional education, training, and experience although these factors may be the immediate cause of the practitioner being able to earn an exceptionally large income. The equivalent factors for a business-man might perhaps be the latest technical devices for customer comfort, mechanical aids, attractiveness of displays etc. but these will usually be represented by monetary investment in tangible assets and thus form part of taxable wealth.

72. No strict equality is thus possible between businesses and professions, because of capital assessment difficulties for the latter. It may be noted however that income tax, which applies to the income actually realised, accords more nearly with equity (on the criterion of ability to pay out of income) than a wealth tax which applies to assessable capital. Such capital inherently produces widely different yields despite the possibly equal output of energy and expertise on the part of the business or professional man. It may be noted however that although in effect each may have an equally valuable business and equal taxable capacity, the professional has less that he can actually transmit to a buyer or by inheritance. The latter point would be material if wealth tax were to be regarded as a substitute for death duties rather than income tax.

: UNQUOTED COMPANIES

73. The goodwill factor referred to above is one of the main difficulties in putting a proper value on the shares of companies which are not quoted on the stock exchange. Stock market prices reflect fairly accurately the propensity of the management of a company to produce corporate income and therefore dividends in excess of the amount which could be generated by a less enterprising deployment of the tangible assets: The difference between the stock market valuation of a company's shares and the value of its tangible assets may amount to a very large figure in the case of the more go-ahead concerns. It is this factor which it is most difficult to value adequately in the case of a private company but which is fully valued in computing the wealth of an owner of quoted equity shares.

74. The other factor in valuing a private company is that the book values of the real property it owns, if entered in the balance sheet at cost, may be quite out of line with market values. This factor may well be allowed for in the share value of a quoted company but would be difficult to deal with in the case of unquoted companies without some requirement for periodical valuations.

: REAL PROPERTY

75. The problems of valuation apply to the whole field of real property. In many countries where some form of taxation is related to real property, valuations are infrequent and taxable values a long way behind current market values (this incidentally is a factor which accounts for the low yield from wealth tax in certain countries and also in the acceptance of the tax despite its inequities). Inequality is inevitable and may be serious in a time of prosperity if the owners of ordinary shares are fully taxed on current market values while the owners of real estate are taxed on low, out-of-date, values.

76. Economic progress depends largely on the willingness of investors to put their money into the equity capital of new and

expanding enterprises. A tax which favours those who keep their money in real estate, therefore may not after all be the encouragement to economic growth it is alleged to be.

: CHATTELS

77. One of the arguments advanced for wealth taxation is that some persons enjoy possessions such as country mansions, landed estates, oil paintings and other works of art which represent a considerable body of capital producing no income and therefore incurring no or negligible income tax, and that it is reasonable to charge some tax accordingly. If taxpayers choose to invest their capital in non-income-producing forms that, it is argued, is no reason why they should pay less tax than someone who employs his capital more productively. The administrative problems, however, of valuing chattels are clearly on a ferocious scale. The sale prices of oil paintings at auctions are rarely predictable with accuracy and are a constant source of journalistic surprise. But this is only one form of artistic chattel, although it is one in which there is at least an active market. Sculptures, antiques, jewellery, collections of rare stamps, match box covers, medals, and other paraphernalia are often extremely valuable but the difficulties of any realistic valuation would be immeasurable. Unless however all chattels of value are brought in to the calculation there can be no equity between different taxpayers.

78. Some countries have simplified their wealth taxes by excluding chattels altogether from the scope of wealth taxation. With the increasing realization that capital gains are nowadays as readily secured from investment in works of art as from other investments, however, more and more wealthy people are investing in this type of asset. To ignore chattels would open the door to avoidance, put a premium on investment in such non-productive assets, defeat the very object of wealth taxation and produce merely a selective wealth tax (see paragraphs 36-38).

UNIVERSAL VALUES

79. Suggested solutions to valuation problems have included allowing the taxpayer to make his own valuation annually which is accepted without question not only for wealth tax but for other purposes including capital gains tax on realisation and for compensation in case of compulsory purchase. This is sometimes known as the system of "universal values". Because, however, capital gains tax may be avoided or indefinitely postponed by not disposing of an undervalued estate and because only a very small proportion of property is compulsorily acquired by Governments, the temptation to under-value and risk the possible consequences is strong.

PRACTICAL SOLUTIONS TO VALUATION PROBLEMS

: INSURANCE VALUES

80. The most practical answer to the valuation problem for chattels is to adopt the figures at which the taxpayer has insured his chattels against the risk of fire and burglary plus of course the estimated value of any uninsured items. This method is far from perfect—assets may be under-insured on out-of-date values—and could in any event only be used in countries where the insurance habit is widespread. The method would thus have little relevance to many developing countries where insurance of chattels is not much practised.

: PERIODICAL VALUATIONS

81. Another solution which has been suggested for valuation problems in general is the method of valuations made, say, at

5-yearly intervals which would then be adopted for the whole 5-year period despite changes taking place during that period. This would remove one of the inequities of general wealth taxation i.e. that real property generally tends to be undervalued (because values are seldom up-to-date) while quoted company shares and other assets held in monetary form can be readily valued at current prices. Assuming that both types of asset are correctly valued at the quinquennial date, the fact that changes in or additions to the holdings of equities and other securities for the following five years were ignored would counterbalance the retention for five years of the value of real estate despite capital appreciation in the interim.

82. It is of interest to note that the fixed "base capital" concept has been adopted in the short-term wealth tax introduced in Chile. The assessment for each of the 3 year's duration 1965, 1966 and 1967 are based on the 1964 capital.[12]) In the case of a "permanent" wealth tax however anomalies might arise from the choice of the quinquennial date.

83. If all taxpayers are assessed on the same base date this provides reasonable equality between taxpayers but involves administrative problems stemming from the burden imposed on valuers and other professionals whose services will be needed to launch the tax. Moreover those who become liable to wealth tax during the course of the quinquennium cannot be given retrospective valuations because they would then be tax-free until the end of the quinquennium.

84. If the valuation dates happen to fall at a time when market values are high, and there is a subsequent recession, although there may be complaints, at least all taxpayers will be "in the same boat" and if the tax proves too burdensome relief can be given by reducing the rate of tax, leaving the values unaltered.

: RELIEF FOR LOSS OF ASSETS

85. The case of the taxpayer whose assets are lost or greatly reduced (e.g. through theft, destruction by fire, business failures) cannot however be left unprovided for in the tax legislation and he would have to be allowed to substitute current for quinquennial valuation.

86. Once exceptions are made to the principle of retaining the same valuation for 5 years these are likely to multiply and there may be scope for evasion by the transfer of assets by A to B such that A then claims the relief of current valuation while B remains content with his previous quinquennial valuation. After the subsequent quinquennial valuation a transfer in the reverse direction would provide further scope for evasion. Quinquennial valuations with different base dates, for example the date a taxpayer's wealth exceeded the taxable limit, would spread the administrative and professional burden but would offer more scope for the transfer type of evasion. In practice one finds that wealth taxes are normally levied by reference to annual valuations although for real estate the values used for some other purpose (e.g. local taxation) are often adopted without adjustment.

: OTHER POINTS

87. Wealth tax has a simple basic concept, the levying of a charge at a low percentage rate on total capital and administrative difficulties therefore centre for the most part on the valuation problems outlined above.

12) Modified only by reference to changes in the value of money during the assessment year, a provision made necessary by inflationary tendencies which might otherwise have seriously eroded the tax yield.

Problems of legal avoidance and illegal evasion are broadly similar to those arising for income tax and similar remedies will apply. For example income tax provisions negating the effect of settlements transferring income to minor children would be appropriate, mutatis mutandis, to deal with settlements of capital. The problems of enforcement (even apart from valuation problems) will in general be more difficult than with income tax, particularly where non-income producing capital is concerned. The flow of income is itself a clue to the existence of capital and where there is no income flow the task of discovery and enforcement of taxation on wealth, particularly where there are no "external indicia", is likely to present difficulties.

CAPITAL LEVIES

DEATH DUTIES

88. The best known form of capital levy is the taxation of a taxpayer's capital by Estate, Inheritance, Legacy or Succession Duties on death. This type of taxation is almost universal and its impact, prima facie, is clearly different from that of a capital levy on the living.

89. Taxpayers who own material amounts of capital like to see it grow, or at least remain intact. They become worried if they feel they are "living on capital" or "eating into their capital"—dead men on the other hand are past worrying.

90. But the living tend increasingly to shew interest in avoiding death duties especially if these are considered onerous. They do so by inter vivos dispositions and other means to ensure adequate provision for their dependants, or to secure survival of a family business or landed estate by removing them as far as possible from the scope of death duties.

91. When death duties apply at fairly high rates the impact may be severe especially in the case of an ultimely death, or a succession of deaths. Tax authorities generally make some abatement in the case of assets which are subjected to several charges of death duties in the space of a few years but there is no general scheme of discounting the duties where the owner of the wealth dies much before the expiration of his actuarial expectation of life.[13])

92. As the need for making some provision for death duties to avoid hardship to the heirs and successors becomes increasingly realised the result, apart from the growth of tax avoidance, is that annual provision tends to be made to meet the ultimate liability.

GIFT TAXATION

93. Where inter vivos gifts are subject to gift taxation this tax either

(a) replaces death duties for the particular assets transferred; or

(b) is treated as a payment on account of death duties, the assets involved being eventually aggregated with those actually passing on death.

94. Gift taxation is usually graduated and where wealthy taxpayers make annual gifts to take advantage of the graduation in the case of a type (a) tax there is perhaps some degree of kinship with an annual wealth tax.

95. The system of making advance provision for death duties may be labelled "pay

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13) Some authorities however exempt or abate death duties where the untimely death was that of a soldier on active duty in defence of his country.

now—die later!" and is in contrast to the example quoted below (para. 117) of the German Equalisation of Burdens Capital Levy which may be described as "Assessment now—pay later!" The significance of both exercises however is the tacit conversion of a capital levy into something akin to an annual wealth tax.

CONVERSION OF DEATH DUTIES TO ANNUAL LEVY

96. We have seen above (paras 15-26) how annual wealth taxes are normally payable out of income. Since in practice many taxpayers continue to make advance provision for death duties (at least on the particular assets they are anxious should be preserved) out of income it is tempting to conjecture whether it would be feasible to convert death duties into an annual tax.

97. It would be relatively easy to demonstrate that there are greater anomalies in the impact of death duties (see, for example, paragraph 91 above) than of an annual wealth tax. It has also been argued above that the incidence of an annual wealth tax is likely on balance to be more anomalous than that of combined taxes on income and capital gains because ability to pay is more accurately measured by income and gains than by the mere possession of capital.

DISINCENTIVE EFFECT OF DEATH DUTIES

98. Although it is popularly accepted that high rates of income and surtax are the main disincentives to economic enterprise it is worthy of consideration whether the replacement of the once-in-each-lifetime levy on capital or a drastic reduction of the rates of the levy would not be an incentive to enterprise which outweighed the disincentive effect of other high direct taxes. This is perhaps more likely to apply to developing countries which sometimes tend to adopt the fairly stringent redistributive tax policies to be found in more developed countries before there has been sufficiently wide generation of wealth to warrant such policies.

99. In reckoning the effects of such a switch in tax emphasis account would have to be taken of the saving in the efforts devoted by taxpayers and their advisers to tax avoidance and by revenue administrators to countering tax avoidance.

100. The loss of tax might be largely made up in time by the higher direct tax yield that would result from the cessation of efforts by testators to divest themselves of capital. Because voluntary re-distribution of wealth to avoid death duties often involves a corresponding decrease in income tax yield, a reduction of these activities would increase the income tax yield.

101. There is another economic aspect i.e. that it is usually better for economic health if assets and wealth can be deployed in what appears to the owner to be the most profitable way, without the distortions involved in tax avoidance manoeuvres. The removal of one major cause of such manouvres shuold have fevourable economic consequences.

102. In many countries death duties produce a comparatively low yield. There is an increasing tendency to abate the rate of death duties,[14]) in some cases there has even been abolition, usually as a means of attracting capital and its owners.

103. Death duties are often a much older (and cruder) tax in a country's fiscal history than income tax and because of the inescapable crudities of incidence are much less cer-

14) The most recent example is Italy where the Finance Minister presented a Bill in April, 1967 to raise the exemption limit from 3 million to 12 million lire and to make certain other concessions.

tain of long survival as taxation grows more sophisticated.

FUTURE PROSPECTS OF DEATH DUTIES

104. Disappearance of the tax base by wholesale avoidance, which in theory is possible in countries without gift taxes, seems however unlikely to occur in practice. For the very human reason that a person who is old and wealthy is more certain of care and attention from his potential heirs than one who is old and poor, the wealthy are unlikely wholly to divest themselves of their wealth before death.[15])

TABLE

(1) National Income		(2) Net receipt of estate duty £ million		Estate duty as percentage of national income
1952	12,716	1952-53	150.6	1.18
1953	13,711	1953-54	160.1	1.17
1954	14,513	1954-55	188.6	1.29
1955	15,388	1955-56	174.4	1.13
1956	16,743	1956-57	167.2	1.00
1957	17,720	1957-58	171.4	.97
1958	18,490	1958-59	186.7	1.01
1959	19,419	1959-60	226.7	1.16
1960	20,706	1960-61	235.9	1.14
1961	22,113	1961-62	261.1	1.18
1962	23,014	1962-63	270.4	1.17
1963	24,212	1963-64	312.4	1.29

Source: (1) National Income Blue Book, 1964, Table 1.
(2) Monthly Digest of Statistics, Table 142.
Hansard, November 10th, 1964.
Written Answers, Column 44.

105. As in the case of taxes on income, very high rates of death duties sharpen the interest in tax avoidance and are undesirable in developing countries as tending to encourage the transfer of wealth and its owners out of the country. In general the yield of tax in such circumstances comes mainly from those who are without direct heirs, are over optimistic about their life-span, or wish to retain full control of all their wealth up to the date

15) "If you are poor, though you dwell in the busy marketplace, no one will enquire about you; if you are rich, though you dwell in the heart of the mountains, you will have distant relatives." (Chinese Proverb). An interesting sidelight on avoidance of death duties was case by the deaths early in 1967 in Britain of lord Fraser and Tony Vandervell. Both were estimated to have "made" about £10 million in their lifetimes but while the Vandervell estate paid tax on that sum, the Fraser estate was only £1.8 million having been reduced by inter vivos dispositions.

of death. Other taxpayers tend, as mentioned, to reduce their liability by inter vivos transfers.

106. The figures for estate duty yield in Britain (see Table), where the duty rates and yield are relatively high despite the absence of gift tax and widespread use of avoidance devices, are a clear indication that death duties are likely to retain a revenue potential for some time to come. Whether that potential will continue to be so fully utilised as time goes on and taxation theories evolve is another question.

107. In the case of Britain, where the death duties yield is larger than in other European countries a factor in shaping the future destiny of the tax may be the need for harmonisation of the tax structure in the event of Britain joining the European Economic Community. At a Conference on Common Market taxation sponsored by the International Fiscal Association in London in November, 1962, Professor Neumark pointed out that wealth taxes and estate duties did not form an important fraction of tax revenues in E.E.C. countries but did in Britain where estate duty provided 3.5% of over-all tax revenue. He went on to say that Britain's entry into the E.E.G. "could not be imagined without a noticeable lowering of her present estate duty."

CAPITAL LEVIES ON LIVING TAXPAYERS

108. It is not proposed in these paragraphs to attempt to assess the economic effects of a capital levy on living taxpayers. Such a levy may vary from a wealth tax which, to a marginal extent, cannot be met from income, all the way to the wholesale expropriation of wealth which has sometimes taken place after a comprehensive change of the political regime in a country. There has however been little, if any, practical experience of capital levies applied as a normal means of taxation in normal times. Experience of capital levies introduced in other circumstances is referred to below.

109. Capital levies may take many shapes other than those mentioned in the previous paragraph. Inflation has been used as a deliberate instrument of capital levy on capital held in the form of Government and other fixed interest securities. Expropriation of business enterprises, particularly where foreign-owned, without, or with inadequate, compensation has been practised on a number of occasions. Such actions are usually on a once-for-all basis—if this characteristic of the levy is not announced by the government concerned, or if an announcement to this effect does not inspire confidence, it is in any event unlikely that a second opportunity for such a levy would occur for a long time.

110. Foreign investors are often willing to take many risks when investing but a demonstrated risk of un-compensated expropriation is the ultimate deterrent to investment. Another (undesirable) form of capital levy is the writing down, usually in times of rampant inflation, of the value of bank deposits and other such cash assets and including larger units of currency without a precisely corresponding diminution in the value of the whole currency.

: EXAMPLES IN PRACTICE

111. A formal capital levy was proposed in Britain after the first World War partly in order to reduce the National Debt the increased size of which caused more concern at that time than it has caused to later generations.

112. The Colwyn Committee appointed in March, 1924 which reported in November 1926 gave serious consideration to the subject of a capital levy. The majority conclusion was that even if such an impost were

well received by the public the relief from public debt likely to be achieved would be insufficient to justify "an experiment so large, difficult and full of hazard". If the levy were not accepted with goodwill "it would be highly injurious to the social and industrial life of the community". The Minority Report of the Committee did not accept this verdict but no capital levy was imposed.

113. After World War II however capital levies were in fact levied in Britain, Germany and Norway, the details varying considerably between the three countries.

BRITAIN

114. In Britain there was considerable Parliamentary discussion during the course of the Second World War about the desirability and feasibility of a capital levy. The Government maintained that such a tax would be administratively difficult. The possibility of transmuting the levy on capital into a tax on income was however mooted by Dr Dalton (later Chancellor of the Exchequer in the postwar Labour Government) who suggested that the rate of income tax and surtax could be increased to 25/−, 30/− or even £2 in the £ (i.e. 125%, 150% or 200%. It was pointed out however that even if a rate of 100% were applied to all incomes over £2,000 the yield would only be £60 million.[16])

115. The eventual upshot of the earlier discussion was the introduction by a subsequent British Chancellor, Sir Stafford Cripps in the 1948 Budget of a levy known as the Special Contribution. This adopted the investment income criteria proposed earlier and imposed a tax, at graduated rates ranging up to a maximum of 50%, for the fiscal year 1948/9 on the investment income of 1947/48 where this exceeded a figure of £250.

116. As the maximum rate of Special Contribution was 50% and the then current maximum rate of income tax and surtax combined exceeded 90%, the liability clearly impinged on capital in the case of wealthier taxpayers faced with tax liability at a maximum total rate exceeding 140% of investment income. This however was a once-for-all levy and not sufficiently heavy (the tax eventually produced a yield of 7.5% of the total yield for fiscal year 1948-49 from income tax and surtax, i.e. £110 m. compared with £1,460 m.) to have caused undue consternation. It seems to have been generally accepted that the tax would not be the subject of an early repetition.

FEDERAL REPUBLIC OF GERMANY

117. In West Germany the capital levy, known as the Equalisation of Burdens Tax, was charged on all property owned on 21 June, 1948. The rate was 50% plus interest and the tax payments could be spread over a period of 30 years from 1st April, 1949. The spreading provisions, even though interest is charged as the price for spreading, clearly soften the impact of the 50% rate very considerably. When allowance is made for the secular decline in the value of money, it can be seen that the tax is not wholly dissimilar in its impact from an annual wealth tax additional to that already imposed at provincial level in Germany.

NORWAY

118. In Norway taxpayers were charged on the increase in their capital as at September 1945 over the capital in 1940 at rates ranging

16) A somewhat similar exercise was done on the occasion of the harmonisation of tax rates in the Malaysian federation in the 1965 Budget. In defending the application of a harmonised top rate of 50% against Opposition attacks the federal Finance Minister, Mr Tan Siew Sin pointed out that for example in Singapore the application of a 100% rate on incomes exceeding $100,000 (£12,000) would produce a mere $2 million (£240,000).

from 20% to 80% after deducting a basic exemption. The increase in capital was of course attributable partly to savings but these would presumably not have been large during the German Occupation and the main targets were the capital gains and the accumulations of wealth made through profiteering and black-marketing during that period.

119. An important factor in the success of this levy (which produced a yield of K 495,000,000) was that popular feeling was very strongly against war profiteers. The administrative basis was also sound since the Norwegian capital tax structure was well established (it was introduced in 1892) and provided the datum capital figures for 1940 with which the 1945 comparison was made.

120. Because the tax was based on the increment of wealth over a period of years it was in a sense more akin to a capital gains tax although it related not to realised gains but to capital growth.

121. The case for a capital levy can only be made out in exceptional times when a large measure of public acceptance is certain and the administrative machinery already exists so that the tax can be imposed swiftly and surely. The three examples of successful capital levies all had these requirements. In Norway and Germany the existing wealth tax apparatus was ready to use and in Britain the income tax machinery was utilised. In all three countries there was the necessary public support in exceptional circumstances.

122. In more normal times and as a general tax measure a capital levy has all the disadvantages of a wealth tax and a few extra ones of its own.

123. The tax only makes sense as a way of obtaining substantial revenue that could not be obtained in other ways. The inequities of incidence of wealth tax which are bearable in the context of low tax rates are by no means acceptable when the rates are substantially increased so that the tax impinges on capital rather than income. This disadvantage applies equally to a capital levy which represents in a sense a compounding of a number of years' wealth tax.

124. Unless there is confidence that the tax will not be repeated (and this is unlikely to be found if the tax is levied in normal times with no "national crisis" justification) the effects are likely to be harmful. Apart from the actual capital drain on enterprises which may cause a contraction of business out of proportion to the amounts actually levied there is the danger of an efflux of capital (as well as of entrepreneurs) to other countries where capital levies are not a part of the fiscal landscape.

125. Such an efflux actually occurred in mainland China when the Government imposed restrictions on the realisation of capital investments with effects broadly similar to that of a capital levy. The movements of capital and know-how to Hong Kong, Taiwan and other countries is now a feature of economic history.

A capital levy is clearly inappropriate to a developing country where the problem is to attract capital by all possible means rather than frighten it away.

CONCLUSIONS

The case for an annual wealth tax on the grounds that wealth has an innate taxable capacity as such is not valid. Where capital produces income there is justification for income tax and where realisations produce capital gains there is a case for capital gains tax. A tax on the mere existence of capital is, however, a capital levy and should be so considered. (See, however, 7 below.)

2. The argument that because wealth tax impinges equally on capital regardless of its income yield it thus encourages the produc-

tive rather than the passive use of capital is not sufficiently valid to warrant adoption of the tax as an economic tool to promote industrial growth. The income yield relative to assessable capital is not necessarily proportionate to the economic desirability of the investment. For example, most desirable investment (in a "growth" sector of the economy) may in fact produce the lowest yield per unit of capital invested and thus suffer more wealth tax than a more conservative investment.

3. In practice (in the countries where the tax is imposed) wealth tax is generally intended to be paid out of income and the impact of the tax is normally modified when the income from particular assets falls below certain limits.

4. Although wealth tax is advocated as a form of incentive as being less oppressive than income tax at the higher rates the impact of wealth tax will be broadly similar. Where income tax (at lower rates) and wealth tax are collected jointly and produce a similar total yield to normal income tax alone no incentive effect is likely to be achieved.

5. To tax higher incomes by reference to the quantum of capital that produces them is likely to prove less equitable in terms of taxable capacity than taxation by reference to actual income produced. Where income produced is roughly proportional to capital employed and therefore to taxable capacity a wealth tax will produce results similar to income tax. Where income from different types of capital varies therefore, the impact of wealth tax will not be proportionate to taxable capacity.

6. The case for some differential between the taxation of earned income and investment income is a valid one but differentiation may be achieved by income tax measures.

7. There is a special case for the taxation of vacant land where its non-development is impeding progress and such taxation constitutes a wealth tax on unproductive capital (strictly a capital levy). This case cannot however be readily expanded into a justification for wealth tax in general.

8. The taxation of wealth in some form has a lengthy history. The principle of wealth taxation is involved where countries determine income tax liability by reference to indicia of wealth, and in taxation of real property and other assets on a selective basis. In addition certain financial measures such as the compulsory restriction of rents and dividends constitute a form of quasi-taxation of wealth. All such selective or quasi-taxes tend to operate unevenly and hence unfairly because they have an impact only on certain elements of wealth and fall lighter on those who have invested their wealth differently.

9. Selective wealth taxes tend to evolve either into taxes on total income or capital or to be replaced by other taxes except where retained as a form of local revenue.

10. Double Taxation treaties involve certain difficulties where one country has only income tax and the other both income tax and wealth tax on the same income-producing assets. The difficulties may be overcome where one country agrees to exempt and leave full taxing rights to the other. In other cases the problem may possibly be met by a transmutation of wealth tax into income tax by deeming the wealth in question to produce a notional level of income.

11. Wealth tax is a basically simple tax being a levy of a small percentage on a taxpayer's total capital. Administrative difficulties centre mainly on valuation, and on the problems of avoidance and evasion which are likely to be greater than for income tax.

12. Anomalies in the administration of wealth tax are likely to arise, for example, in the treatment of business and professional goodwill, annuities and pensions, stocks, sha-

res and gilt-edged securities, and of chattels.

13. Because of the need to keep administrative costs within limits valuations, for example of real property are likely to be based on figures which are subject only to infrequent review. If other assets such as stocks and shares are brought in at current market value there will be anomalies in times of rising price levels between owners of different forms of wealth. To value all assets, say, quinquennially produces other problems and anomalies.

14. Because of the anomalies referred to above it is difficult to demonstrate that wealth tax is superior to income tax even from "incentive" aspect. In countries where the tax already exists however it may well survive for some time either for political reasons, or, in cases where it provides local revenue, for the lack of alternatives.

15. Capital levies or "death duties" on the assets left by a deceased taxpayer are operated in a large number of countries. Prima facie such as duties have the least possible disincentive effect because they are levied on the dead. In practice the living tend increasingly to make provisions to avoid or reduce death duties and secure untaxed transfer to their heirs of family assets.

16. Except for the abatement of duties where assets are taxed several times within a few years because of a succession of deaths, the taxes payable on death are not related to the life-span so that the impact is uneven where equal estates are owned by different persons whose length of life varies materially. In this respect an annual wealth tax in substitution for the larger once-in-a-lifetime tax would obviously be superior but as already noted wealth tax has its own anomalies.

17. There is a current tendency for the rates of death duty to be decreased and in most countries the yield is comparatively small. An exception is Britain where the rates and the yield are high, the latter despite widespread avoidance manoeuvres and the absence of gift duty. The future will probably bring further reductions in duty rates coupled with better enforcement and there are factors which make it unlikely that avoidance measures will even be taken to such extremes as to reduce the death duty yield to extinction.

18. Capital levies on living taxpayers, including measures such as un-compensated expropriation, are comparatively rare. Examples of formal capital levies are those imposed in Britain, Germany, and Norway after World War II which differed appreciably in detail but were each made in circumstances of general public support in the aftermath of a bloody and costly war. Such levies are not in practice encountered in normal times as a method of raising ordinary revenue.

19. In a developing country an important consideration is to encourage the generation and accumulation of capital and to attract entrepreneurs and the owners of capital. In such circumstances a capital levy is unlikely to be an appropriate method of raising revenue because of the disincentive effect on present and potential investment.

APPENDIX

Brief details of wealth taxes in selected countries

	Rates	Exemption	Notes on Scope etc.
Argentina	1%	P. 300,000 (married taxpayer)	Emergency Tax on Immovable Property

Ceylon	0.5 to 2.0	Rs. 100,000	
Denmark	0 to 2.3	Kr. 200.000	
Federal Republic of Germany	0.75 to 1.0	Dm 40,000 (married taxpayer)	
Guatemala	0.6		
Guyana	Tax on undeveloped land proposed in Budget of 17.1.67		
Holland	0.6	F. 55.000 (Married taxpayer)	Rate increased to 0.6 for Period 1966-1969
India	0.5 to 2.5	Rs. 100,000	
Indonesia	0.5	Rp. 500,000	
Japan	0.5 to 3.0		
Luxembourg	0.5	Fr. 100,000	
Norway	05. to 1.75	Kr. 30.000	+ local wealth tax
Pakistan	1.0 to 2.5	Rs. 400,000	
Philippines ("Residence Tax B")	0.04	P. 10,000	(Maximum Tax = P. 1000)
Sweden	0.8 to 1.8		Kr. 100.000
Switzerland	0.0625 (Federal) 0.15 to 0.5 (Cantonal)		
Taiwan	0.6	N.T. $6,000	

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P.L. JAITLY*):

TAX LIABILITY OF FOREIGNERS ON BUSINESS TRANSACTIONS IN INDIA

CHARGE OF INCOME-TAX:

Chargeability of income-tax arises under section 4 of the income-tax Act, 1961, which reads as under:—

"(1) Where any Central Act enacts that income-tax shall be charged for any assessment year at any rate or rates, income-tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of, this Act in respect of the total income of the previous year or previous years, as the case may be, of every person:

Provided that where by virtue of any provision of this Act income-tax is to be charged in respect of the income of a period other than the previous year, income-tax shall be charged accordingly

(2) In respect of income chargeable under sub-section (1), income-tax shall be deducted at the source or paid in advance, where it is so deductible or payable under any provision of this Act."

From the above it would appear that income-tax is chargeable for the assessment year in respect of the total income of the previous year except in certain specified cases. It is, therefore, necessary to consider the meanings and scope of the terms:

(1) total income,
(2) previous year, and
(3) assessment year.

WHAT IS TOTAL INCOME?

The expression "total income" is defined in section 2(45) to mean the total amount of income referred to in section 5, computed in the manner laid down in the Act. There are, however, items of income which are exempt from tax and thus not liable to be included in computing the total income. These are enumerated in sections 10 to 13 (Chapter III). The term "total world income" was defined by section 2(46) to include income wherever accruing or arising, except incomes which are not included in the total income under any of the provisions of Chapter III (relating to incomes which do not form part of total income) and except any capital gains which are not included in the total income of an assessee. This sub-section has been deleted by the Finance Act, 1965, and, therefore, now the expression "total world income" does not find its place in the Income-tax Act. Section 113 regarding tax payable by or on behalf of non-residents has also been omitted. As a consequence of this change, it is no more necessary for a non-resident individual to exercise the option of being taxed on the basis of total world income by filing a written declaration with the Income-tax officer before 30th June of the assessment year in which he first became assessable as a non-resident or otherwise pay tax at the minimum rate of 48.37%. The rates of tax now for

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residents and non-residents are alike except that the minimum income exemption and marriage and children allowances are not available to non-residents although they are applicable to not ordinarily residents. The loss of these reliefs is, however, immaterial as compared to the disadvantage of being taxed at a very high minimum rate.

Different rates of tax for the purpose of deduction at source have been separately provided for non-residents but they can claim refund of tax if their tax liability is lower because of the lower total income, by filing income-tax returns in the prescribed manner.

SCOPE OF TOTAL INCOME:

According to section 5 of the Income-tax Act, the following incomes of the previous year shall be taxable depending upon whether a person is a resident, non-resident or not ordinarily resident.

1. In the case of a resident:
(a) Income received in India by him or on his behalf.
(b) Income deemed to be received in India by him or on his behalf.
(c) Income which accrues or arises in India.
(d) Income which is deemed to accrue or arise in India.
(e) Income which accrues or arises outside India.

2. In the case of a non-resident:
(a) Income received in India by him or on his behalf.
(b) Income deemed to be received in India by him or on his behalf.
(c) Income which accrues or arises in India.
(d) Income which is deemed to accue or arise in India.

3. In the case of residents, but not ordinarily residents:
(a) Income received in India by him or on his behalf.
(b) Income deemed to be received in India by him or on his behalf.
(c) Income which accrues or arises in India.
(d) Income which is deemed to accrue or arise in India.
(e) Income which accrues or arises outside India if derived from a business controlled or a profession set up in India.

An income can be taxed only once and, therefore, if it has been taxed on accrual or arising or deemed accrual or arising basis, it cannot be taxed again on the ground of receipt or deemed receipt, either in that year or in any other year. This injunction finds express mention in explanation 2 to section 5.

RESIDENTIAL STATUS:

From the above analysis, it would appear that assessees, irrespective of being Indian or Foreigner, are classified into three residential categories, namely:—

1. Ordinarily residents (known as "resident").
2. Not ordinarily residents.
3. Non-residents.

The classification is determined in each case for each previous year according to the technical definition set out in section 6 and not by the ordinary meaning of the term.

If a person is resident in India in a previous year relevant to an assessment year in respect of any source of income, he shall be deemed to be resident in India in the previous year relevant to the assessment year in respect of each of his other sources of income.

DISTINCTION BETWEEN "FOREIGNERS" AND "NON-RESIDENTS".

Before considering the income-tax liability of foreigners in India, it is important to draw distinction between a "foreigner" and a "non-resident". "Non-resident", as defined in sub-section 30 of "section 2 of the Income-tax Act, 1961, means a person who is not a "resident" and for the purposes of sections 92, 93 & 168, includes a person who is not ordinarily resident within the meaning of sub-section (6) of section 6.

The term 'foreigner' which is not defined in the Income-tax Act, means a person who is not a citizen of India. A foreigner may become a resident for the purpose of Indian Income-tax Act in a particular year in view of the technical definition of the term. Similarly, an Indian may become a non-resident or not ordinarily resident depending upon the period of his stay in India during the previous year and the years preceding. The main difference between a 'foreigner' and an Indian 'non-resident' is that whereas the former is entitled to certain exemptions provided in section 10 (6) of the Income-tax Act, they are not available to the latter. Moreover a foreigner who comes to India can leave the country only on production of the tax clearance certificate issued by the Income-tax Department after satisfying that the taxes due from him have been paid or arrangements satisfactory to the Department have been made for payment of such taxes after his departure from India. This restriction is not applicable to an Indian even though he may be a 'non-resident' within the meaning of the Income-tax Act unless he is leaving the country without any intention of returning.

DISTINCTION BETWEEN "RESIDENTS" AND "RESIDENTS BUT NOT ORDINARILY RESIDENTS:"—

A person who is resident but not ordinarily resident enjoys better position than a resident for the purposes of income-tax liability in India in as much as his income accruing or arising in a foreign country is taxable only if it is derived from a business controlled or a profession set up in India. On the other hand, a resident who is also ordinarily resident is liable to tax in respect of all his foreign income whether or not it accrues or arises in India.

DISTINCTION BETWEEN "RESIDENTS BUT NOT ORDINARILY RESIDENTS" AND "NON-RESIDENTS".

Residents but not ordinarily residents are liable to tax on income accruing or arising to them outside India if derived from a business controlled or a profession set up in India. Such income, however, is not taxable in the hands of non-residents.

RESIDENCE OF AN INDIVIDUAL:

According to the provisions of section 6 of the Income-tax Act, an individual is said to be resident in India in any previous year, if he satisfies one of the following conditions:

1. He is in India in that year for a period or periods amounting in all to 182 days or more.
2. He maintains or causes to be maintained for him a dwelling place in India for a period or periods amounting in all to 182 or more in that year and has been in India for thirty days or more in that year.
3. He is in India for sixty days or more in that year and had also been in India for an aggregate period of 365 days or more within the four years preceding that year.

NOT ORDINARY RESIDENCE:

As individual is considered to be not ordinarily resident in India in any previous year unless the following two conditions are satisfied.

1. He had been resident in India in nine out of ten previous years preceding that year.

2. He had been in India for a period or periods amounting in all to 730 days or more during the seven previous years preceding that year.

It may be important to mention here that the term "resident but not ordinarily resident" is applicable to individuals and Hindu undivided families only. It is not relevant to companies, firms, associations of persons and bodies of individuals.

RESIDENCE OF A COMPANY:

A company is said to be resident in India in any previous year if:

(i) it is an Indian company; or

(ii) during that year, the control and management of its affairs is situated wholly in India.

An Indian Company, that is a Company incorporated under Indian Law, will always be considered as resident even though the control and management of its affairs may be situated wholly outside India.

In the case of a Company incorporated outside India, it will be treated as resident only if the control and management of its affairs is situated wholly in India. Even a minor part of the control and management outside India will render it as non-resident.

RESIDENCE OF A FIRM, AN ASSOCIATION OF PERSONS AND A BODY OF INDIVIDUALS

A firm, an association of persons or a body of individuals is said to be resident in India in any previous year in every case except where during that year the control and management of its affairs is situated wholly outside India. Thus, even a minor part of the control and management of these categories of assessees in India is sufficient to treat them as residents. In fact it is difficult to imagine a firm, an association of persons or a body of individuals functioning in India to be non-resident.

CONTROL AND MANAGEMENT:

Control and management is said to be located at a place where the head and brain of the trading adventure is situated. The place where the trading activities or physical operations of a business are carried on may not necessarily be the place of control or management. Take the case of a Corporation. It may be incorporated in place A, have its manufactory at place B and yet its control and management may be situated at place C. That would be so if the directive power, the head and brain, are situated at place 'C'. If the board of directors of a Corporation casually hold their meetings at a particular place, that may not necessarily be the situation of their directive power, the head and brain. There must be functioning of such power at a place with some degree of permanence.

ASSESSMENT YEAR AND PREVIOUS YEAR:

"Assessment year" is defined in section 2(9) to mean the period of 12 months commencing on the first day of April every year. The method of taxation under the Indian Income-tax Act is that the actual income of the "previous year" is taxed in the assessment year. The assessment year is the year for which tax is paid on the total income of the previous year. "Previous year" which has been defined by section 3, may either be the financial year (the year ending 31st March) or any other period except in the case of income from salaries, interest on securities and presumptive income from real property when the financial year alone can be adopted as the previous year. Thus it is open to an assessee with income from business or profession or from other sources to make up his accounts to any day other than the last day of the financial year." In that case the previous year will be the period consisting of 12 months or less ending on such day. In

other words, if an assessee starts his accounts on 1st July, 1967, his previous year will be either the 12 months ending 30th June, 1968 and the assessment year 1969-70 or the period ending 31st March, 1968-69 as the assessment year. If he choses to close his previous year on any other date before 30th June, 1968, the assessment year will be 1968-69 if the accounts are closed on or before 31st March, 1968 and 1969-70 if closed after 31st March but on or before 30th June, 1968.
An assessee can have different previous years in respect of separate sources of income.
For change of previous year the permission of the Income-tax Officer is necessary under section 3(4). The Income-tax officer, may, while according sanction, impose such conditions as he may think fit. If permission to change the previous year is declined, such order will not be appealable.

RATES OF TAX:

The rates of tax to be levied on the income of a previous year are those rates in force in the assessment year as prescribed by the Finance Act. In the case of income from salaries, however, the rates of the previous year are applicable. The Finance Minister presents the country's Budget before the Parliament in the form of Finance Bill in the end of February every year which takes the shape of Finance Act in the month of May, except in the election year when the presentation is delayed by about three months. 1967 being the election year, the Budget was presented on 25th May. (The election takes place every fifth year).
The rates of tax prescribed in the Finance Act, 1967, will apply to all previous years closing on or before 31st March, 1967. Even a previous year ending 30th April, 1966 will be subject to the rates of the Finance Act, 1967 because it will be relevant to the assessment year 1967-68. In the case of income from salaries, however, the rates prescribed in the Finance Act, 1966, will apply to the previous year ending 31st March, 1967.

TAXABLE ENTITIES:

Tax payers, known as assessees in the income-tax nomenclature, are classified into following categories:—
1. companies,
2. individuals,
3. Hindu undivided families,
4. local authorities,
5. firms,
6. associations of persons or bodies of individuals, whether incorporated or not, and
7. artificial juridical persons, not falling under any of the preceding categories.

Among the above, only the following are relevant to foreigners:—
1. companies,
2. individuals,
3. firms,
4. associations of persons, and
5. bodies of individuals.

They are briefly discussed below:—

COMPANIES:

A company under the Income-tax Act is defined in sub-section (17) of section 2 as under:—
"Company" means:—
(i) any Indian company, or
(ii) any association, whether incorporated or not, and whether Indian or non-Indian which is or was assessible or was assessed under the Income-tax Act, 1922, (11 of 1922), as a company for the assessment year commencing on the first day of April, 1947, or which is declared by general or special order of the Board to be a company for the purpose of this Act.
A foreign company will be treated as an "association of persons" unless it is declared as a company by the Central Board of

Direct Taxes for which purpose an application has to be made to the Board. This will affect the rates of tax which are different for different categories of assessees. In the case of Companies, the rate varies between 45% and 65% depending on various conditions.

INDIVIDUALS:

The term "individual" means a natural person i.e. a human being and not an artificial juridical person. It includes a minor or a person of unsound mind in whose case the assessment may be made on the guardian or trustee of the minor or lunatic.

The rates of tax applicable to individuals, associations of persons and bodies of individuals are the same and ranges between 5% and 65% on slab-basis plus a surcharge of 20 to 25% on income-tax in the case of unearned income in certain specified circumstances and a special surcharge at the rate of 10%, both on income-tax and surcharge.

FIRMS:

The expression ,,firm" has been defined by section 2(23) of the Act according to which, it has the same meaning as assigned to it in the Partnership Act, 1932. An extended definition has been given to the word ,,Partner" by section 2(23) by including any person who, being a minor, has been admitted to the benefit of partnership. Partnership is the relationship between partners who have agreed to share profit or loss of a business carried on by all or any one of them acting for all. There must be at least two major partners to constitute a firm. Carrying on of a business is a necessary requisite of partnership. Partners may carry on business personally or through servants or agents. Whether a particular relationship constitutes partnership is to be determined having regard to the terms and conditions governing the constitution thereof. The name given to it by the parties is not decisive of the issue. In some cases one finds a number of restrictions imposed on one partner and many extra powers given to another. A particular partner may be entitled under the partnership instrument to conduct the entire business at his sole discretion. Such powers would not be destructive of the validity of partnership.

DISTINCTION BETWEEN PARTNERSHIP AND CO-OWNERSHIP:

Partnership must be distinguished from co-ownership of property. Co-owners are taxed on their individual shares of profit in the property while partnership is assessed as a unit. The total income of a registered firm is divided amongst its partners in accordance with their respective shares in the profit of the firm as provided in the instrument of partnership. Such income is added to the other income of every partner and taxed determined on the individual rates of tax on the income so arrived at. Besides these taxes, a tax at the following rates is payable by the firm on its income:

(1) Where the total income does not exceed Rs 25,000.	.. nil
(2) Where the total income exceeds 25,000, but does not exceed Rs 50,000.	.. 6% of the amount by which total income exceeds Rs 25,000.
(3) Where the total income exceeds 50,000 but does not exceed Rs 1,00,000.	.. Rs 1500 + 8% of the amount by which the total income exceeds Rs 50,000.
(4) Where the total income exceeds Rs 1,00,000.	.. Rs 5,500 + 12% of the amount by which the total income exceeds Rs 1,00,000.

PARTNERSHIP BETWEEN COMPANIES

A Company being a separate legal entity, can constitute a partnership firm with other companies and/or individuals. But a firm not being a legal person cannot, as such, enter into a partnership.

ASSOCIATION OF PERSONS:—

Where two or more persons join together to carry on a business for profit, they will be assessible as 'an association of persons'. An association of persons will be subject to tax at the same rates as an individual. A resident association of persons is liable to pay annuity deposit in the same way as an individual, but the Annuity Deposit Scheme, is not applicable to non-resident individuals or associations of persons. Before a unit can be taxed as an association of persons, it is necessary that the income should be the result of a joint act or a joint venture. In C.I.T. v: Indira Balkrishna (1960) 39 I.T.R. 546, the supreme court has laid down that to constitute an association of persons, there must exist common purpose or common action for producing income. Distinction between 'association of persons' and 'co-owners' should be borne in mind. Persons who join in common purpose with the object to produce income would constitute an association of Persons (Mohammad Noorullah v. C.I.T. (1961)42 I.T.R. 11 5(S.C.). In the case of co-owners of property, they may be treated as an association of persons if their shares are not definite and ascertainable, but otherwise assessment will be made on each owner with respect to his definite share. This is so because mere co-ownership is not sufficient to constitute an association of persons. If on the other hand, there exists an indication of joint enterprise amongst co-owners, they would be assessed as an association of persons. This rule however, is subject to the provisions of section 26 with the result that in case of house property, to which alone the said section applies, the tax would be levied individually on the co-owners provided they have their individual shares precisely defined and that would be so though the property may be managed and owned jointly by them.

ILLEGAL ASSOCIATIONS:

More than ten persons in the case of banking business and twenty in the case of any other business cannot carry on business unless they get themselves incorporated as a company. But if more than the above number of persons join in common venture, they would be taxable as an association of persons, because illegality in the constitution of an association of persons would not affect its liability to tax. (Mohamad Abdul Kareem & Co. v: C.I.T. 1948 I.T.R. 412). The same would be the position with respect to any illegal partnership.

BODIES OF INDIVJDUALS;

In section 2(31) of the Income-tax Act, 1961, the words "body of individuals" have been added in clause 5 after the "association of persons" which did not exist in the 1922 Act. It appears that the intention of adding these words is not to tax co-ownerships with defined shares as associations of persons, though persons like executors representing an estate jointly may now fall within the expression "body of individuals".

DIFFERENT CATEGORIES OF INCOME:—

According to section 14 of the Income-tax Act, all income shall, for the purpose of income-tax and computation of total income, be classified under the following heads of income:—

1. Salaries.
2. Interest on securities.
3. Income from house property.

4. Profits and gains of business or profession.
5. Capital gains.
6. Income from other sources.

For the purpose of this article, the following incomes are relevant to foreigners:

SALARIES:

(1) Salaries of foreigners visiting India on tour of duty.
(2) Salaries of foreign technicians employed in India.

PROFITS AND GAINS OF BUSINESS:

1. Income from sale of machinery, equipment and other goods in India.
2. Income from purchase of goods in India.
3. Income from installation of machinery in India.

INCOME FROM OTHER SOURCES:

(1) Income from interest on machinery supplied at credit.
(2) Income from dividends.
(3) Income from royalties and technical fees.

Each type of income stated above is discussed below separately.

SALARIES OF FOREIGNERS VISITING INDIA ON TOUR OF DUTY

Foreigners visiting India on tour of duty are generally employees of foreign concerns. They come to study the Indian market, to introduce their employers' products in India of as lent officers of the Indian agents of their employers for rendering technical advice or supervising erection. The remuneration received by them as employees of foreign enterprises for services rendered during their stay in India is exempt from Indian tax under Section 10(6)(vi), provided the following conditions are fulfilled:

(a) the foreign enterprise concerned is not engaged in any trade or business in India,
(b) stay of the foreigner concerned in India does not exceed in the aggregate a period of ninety days in such previous year, and
(c) such remuneration is not liable to be deducted from the income of the employer chargeable under this Act.

It appears that the period of ninety days is to be reckoned in each previous year. For example, if an individual reaches India on the first of January, 1967 and stays upto 29th June following, he would have stayed in India for ninety days in each of the two previous years ending 31st March, 1967 and 31st March, 1968 though the total period of of his continuous stay aggregates to six months. His remuneration for six months will, therefore, be exempt from Indian tax subject to the satisfaction of other conditions mentioned before.

SALARIES OF FOREIGN TECHNICIANS EMPLOYED IN INDIA

It is provided in section 10(6) (vii) of the Income-tax Act that the remuneration of a foreign technician received by him for services rendered to the Government, a local authority, any corporation set up under any special law or a business carried on in India, is exempt from tax for one year without Government approval and for three years if his service agreement is approved by the Government either before the commencement of service in India or within one year of such commencement. It is, however, an important condition of the exemption that the foreign technician should not have been resident in India in any of the four financial years immediately preceding the financial year in which he arrived in India. It is also necessary that the technicians coming to India should satisfy the definition laid down in the explanation to section 10(6) (vii) of the Income-tax Act to be entitled to the exemption. The said explanation is re-produced below for the sake of ready reference:

Explanation—"Technician" means a person having specialized knowledge and experience in—
(i) constructional or manufacturing operations, or in mining or in the generation or distribution of electricity or any other form of power, or
(ii) industrial or business management techniques;
who is employed in India in a capacity in which such specialised knowledge and experience are actually utilised".
After the expirty of the aforesaid three years, a technician can be employed for further five years with the approval of the Central Government on the condition that the tax chargeable on his salary shall by paid by the employer to the Central Government. In the case of technicians with special knowledge and experience in industrial or business management techniques, the exemption of tax on salary is available only for six months.

INCOME FROM SALE OF MACHINERY, EQUIPMENT AND OTHER GOODS IN INDIA:
As the tax liability of a foreign supplier in India arises either on accrual or arising or deemed accrual or arising basis or on receipt or deemed receipt basis, it is important to observe the following precautions while executing an agreement:
1. In the case of supply of machinery, equipment and other goods it should be stipulated in the agreement that the delivery of goods shall be effected in the foreign country so that no income or profits accrue or arise in India.
2. In the case of an agreement for supply of know-how all documents in the shape of drawings, designs and blue prints should be supplied by the foreigner in the foreign country so that the property therein passes outside India without attracting the Indian tax liability on the basis of accrual or arising of income or profits in India.
3. Payments against supply of machinery and know-how should be received outside India so that no tax liability arises on the basis of receipt of income or profits in India. Here it is important to understand what is deemed accrual or arising or deemed receipt of income in India.

INCOME DEEMED TO ACCRUE OR ARISE OR DEEMED TO BE RECEIVED IN INDIA
Section 9 introduces a fiction and deems certain income, otherwise accruing or arising without India, to have accrued or arisen in India. The fiction will not operate if income otherwise accrues or arises in India. (Turner Morrison & Co. Ltd. v. C.I.T. (1953) 23 I.T.R.152 (s.c.). As has been discussed already, proviso to section 5 excludes from taxability income accruing or arising to a person not ordinarily resident unless the same is derived from business controlled or profession set up in India. The fiction introduced by section 9 will affect the ambit of this proviso also. Consequently, if income is deemed to accrue or arise in India by virtue of section 9, the proviso to section 5 will be of no avail to a person not ordinarily resident. Income deemed to be received means income not in fact received but treated fictionally by the statute to have been received. For instance, the dividend paid by an Indian Company outside India is not in fact received in India but is deemed to be received in India, and, therefore, taxable.
It is quite evident that in order to save a transaction of sale from the net of taxation in India, the delivery of goods must be effected outside India and the price also received outside. If the machinery is delivered in India, the profits accure in India and are, therefore, subject to Indian tax. On the other hand, even though the machinery is delivered outside India, but the price is received in India, the profits are taxable in India on

receipt basis. But here it is important to note that the delivery of goods outside India is not the sole creterion to establish that no profits accrued or arose in Indian. A foreigner may earn profits through an agent. Under section 163, the Income-tax officer is empowered to treat any of the following persons as agent of a non-resident.

1. A person employed by or on behalf of the non-resident; or
2. a person having any business connection with the non-resident; or
3. a person from or through whom the non-resident is in receipt of any income, whether directly or indirectly; or
4. a person who is the trustee of the non-resident.

In sub-section (1) of the said section, it has been clarified that a broker in India who does not deal directly with or on behalf of a non-resident principal in respect of any transactions but deals with or through a non-resident broker shall not be deemed to be an agent provided the transactions are carried on through him in the ordinary course of business and the non-resident broker carries on such transactions in the ordinary course of business and not as a principal. It is, further important to note that an agent is liable to be charged only on such income as accrues to the non-resident through dealings with him and not in respect of income accruing or arising to the non-resident with which the agent has no concern. Thus it would appear that an agent of a non-resident in India may not necessarily be the agent for all his business transactions in that country. There may be different agents for different deals and in certain cases there may be no agent at all, for instance, when the business is transacted on principal to principal basis. If a foreigner sells goods in India as principal to principal, he does not incur Indian tax liability on accrual basis because the importer, in such a case, cannot be held to be an agent of the exporter within the meanings of section 163 of the Income-tax Act. What is a "principal to principal" transaction has been explained in circular No. 17(XXXVII-1) of 1953 No. 26(26) I.T./53 dated 17th July, 1953 of the Central Board of Revenue (now Central Board of Direct Taxes) reproduced below:

"Non-resident exporters— Where the transactions of sales and purchases are as between principal to principal, no liability of the exporter arises in India on accrual basis, and the resident importer cannot be held to be the agent of the exporter on the basis of such transactions. It is difficult to lay any hard and fast criteria for determining whether the transactions are between principal to principal. The real relation between the parties will have to be looked into from any agreement existing between them, but where—

(a) the purchases made by the resident are outright on his own account,

(b) the transactions between the resident and non-resident are made at arms-length and at prices which would be normally chargeable to other customers,

(c) the non-resident exercises no control over the business of the resident and sales are made by the latter on his own account, or

(d) the payment to the non-resident is made on delivery of documents and is not dependent, in any way, on the sales to be effected by the resident,

it can be inferred that the transactions are as between principal to principal"

BUSINESS CONNECTION

The term 'Business Connection' has not been specifically defined in the Income-tax Act, but it denotes an element of continuity in the relationship between the non-resident who earns profits from business operations in India and the person in India who assists in

earning such profits. The profits, however, must be attributable to the operations carried on in India. In case business connection is established in India, a reasonable portion of the amount involved in business connection will be treated as profit accrued or arisen in India. A business connection may be held in the following cases:

1. Where a non-resident maintains a branch office in India for transacting business.
2. Where an agent is appointed in India for business purposes.
3. Where there is a close connection between a resident and non-resident.
4. Where there is a close financial association constituting business relationship between a resident and non-resident.

It has, however, been held in Turner Morrison v. C.I.T., (1953)-23 I.T.R. P-152, that where only a part of the sale proceeds is received in India, only a part of the profits will be regarded as received in India. Thus,in respect of goods supplied by a foreigner on F.O.B. a foreign port basis so that no income accrues or arises in India, if he received 80% of the price abroad and 20% in India, profits attributable to 20% only will be subject to Indian tax.

In a recent case decided by the Supreme Court (C.I.T.v.R.D. Agarwal & Co. and another (1965)-56 I.T.R.20), the facts were that the assessee canvassed orders from dealers in Amritsar for the supply of goods and communicated to certain non-resident exporters having no authority himself to accept on behalf of the non-residents. Orders were accepted by the non-residents, price received by them and delivery also given outside the taxable territories. No operation such as procuring raw materials for manufacture of finished goods took place within the taxable territories. The assessee was only entitled to certain commission on the sales. It was held that there was no business connection within the meaning of section 42(1) of the Income-tax Act, 1922 (corresponding to section 160 of the Income-tax Act, 1961) of the assessee with the non-residents and the assessee, therefore, could not be treated as an agent of the non-residents for the purpose of taxing the profits that accrued to them from their export business.

SALES AGAINST TENDERS

A sale against tenders may be made either on self-buyer basis or on behalf of a foreign principal. Where an Indian trader buys goods from a foreign manufacturer on principal to principal basis and imports them on his own account, it will be considered as a self-buyer transaction. In a self-buyer business, the foreign supplier does not incur tax liability in India provided the goods were delivered and the price received outside India. But it is advisable that in such a case, the supplier should charge net price after deducting discount and draw invoices accordingly. The importer may then sell the goods to his customer on the price tendered by him. As the Indian buyer purchased goods on principal to principal basis and sold them on his own account, the foreign seller does not come into the picture. But the position would be quite different if the Indian purchaser sold the goods in India on the same price at which he imported them. In such a case, the Income-tax Department may hold that the business was carried on between the Indian party and the foreign party in close connection resulting in indirect profits to the non-resident within the meaning of section 92 of the Income-tax Act, thus involving the foreign party in tax liability through the Indian party as agent.

Alternatively, if the Indian representative completes tenders on behalf of the foreign manufacturer with the latter's authority to

do so and submits to the prospective purchaser, he will be deemed as an agent of the foreign manufacturer. Consequently if the tender is accepted, the profits on the transaction will be taxable in India on accrual basis, even though the payment is made outside India. If, however, the Indian representative just delivers the tenders in India, received by him from the foreign party duly signed and completed, without authority to make commitments on behalf of the latter, he will not be regarded as an agent. In this connection reference may also be invited to the Board's letter No.F.56(5) I.T/48 dated 21st June, 1949 in which it was laid down that where a resident commission agent who purchases goods for or on behalf of a non-resident principal, shows in his accounts a net profit of at least 3%, no attempt should be made to assess the non-resident principal under section 42(2) of the Income-tax Act, 1922 (corresponding to section 92 of the Income-tax Act, 1961). Now, on representation, the Board has decided that the criterion of 3% need not be applied in future if it is clear that the resident person acts in the usual course of business in making purchases for the non-resident party. In such a case, no attempt should be made to treat the resident commission agent as an agent of the non-resident party merely on the ground that the net profit shown by the party is less than 3%. The same principle should apply in the case of a resident commission agent making purchases for or on behalf of a resident from a non-resident. It is, however, necessary to show a reasonable profit, as otherwise section 92 will be attracted.

ALLOTMENT OF SHARES AGAINST SUPPLY OF MACHINERY OR KNOW-HOW

In certain cases, foreign collaborators agree to accept allotment of shares against supply of machinery or supply of know-how with the stipulation that the share certificates will be delivered outside India. The machinery or know-how, as the case may be, is supplied outside India so that no income or profits accrue or arise in India. In order to avoid tax liability on receipt basis, the share certificates in respect of the shares agreed to be allotted in consideration of the value of machinery or know-how, are also stipulated for delivery outside India. It may be pointed out that in these circumstances, although no tax liability of the foreigner will arise in India in respect of the supply of machinery or know-how, yet the allotment of shares will amount to payment of their price in kind in India in the shape of shares. The delivery of certificates outside India will not change the situation. The allotment of shares takes place at the registered office of a company and that is exactly the place where the shares are deemed to be received by the allottee. It is important to understand this position clearly to avoid any misapprehension.

PLACE OF AGREEMENT

It is important to bear in mind that an agreement for supply of machinery, equipment or know-how or any other collaboration agreement should always be executed outside India to avoid the possibility of any income being treated to have accrued or arisen at the place where the agreement is signed. The premises of a foreign country's embassy in India are deemed to be a foreign territory and, therefore, it is believed that an agreement signed in the precincts of an embassy will be treated to have been executed outside India.

INCOME FROM PURCHASE OF GOODS IN INDIA

The position of taxability in the case of income from purchase of goods in India for the purpose of export has changed since 1964. The Finance Act 1964 introduced an amendment to section 9(1)(b) as a result of which it has now become clear that a non-resident is not liable to tax on any income derived from purchase of goods in India for export, even if he keeps an office or agency in India for the purpose.

INCOME FROM INSTALLATION OF MACHINERY IN INDIA

Sometimes foreigners undertake to supply machinery in India as well as to instal it. Here it is important to note that the supply of machinery and its installation should form two separate contracts. If both the transactions are clubbed together in one contract, there is a possibility that the profits from sale of machinery derived in India as well as the profits from erection contract may be subjected to Indian tax. The Income-tax Officer, in such a case, may hold that the foreigner undertook to supply machinery duly installed in India. It is, however, possible to execute two contracts under one document, but it needs careful drafting. If separate contracts are executed, the supply of machinery will not be subject to Indian tax provided necessary precautions regarding delivery and payment outside India are observed. The question will then narrow down to the consideration of the taxability of profits from erection contract only. If the supplier of machinery undertakes its erection, it will amount to carrying on business in India and profits earned on the contract will be liable to Indian tax. If, however, the contract does not result in profit, there will be no tax liability. In such cases it would be advisable to maintain separate books of accounts and open separate bank accounts to work out exact profit or loss from each contract. If it is not so done, the Income-tax Officer shall estimate taxable profit to the best of his judgment. In the absence of proper accounts records, the circumstances may lead him to estimate profit even though in fact there may be a loss. To avoid such a contingency, the maintenance of proper books of accounts is very important. It may be possible to arrange the erection of machinery in India in such a way that no tax liability of the foreing supplier arises. For this purpose separate agreements between the Indian purchaser and the foreign supplier should be entered into as under—

(1) An agreement for supply of know-how in the shape of drawings, designs and blue prints etc. for the erection of machinery.

(2) An agreement for the loan of services of technicians to undertake erection.

The know-how material viz. designs, drawing and blue prints etc. should be supplied by the foreigner to the Indian party outside India at the agreed price and the payment should also be received outside. For supplying know-how outside India, drawings etc. may be delivered to a representative of the Indian party in the foreign country. In such an event it will be deemed that the delivery of know-how was effected outside India on behalf of the Indian party and, therefore, no income or profits accrued or arose to the foreigner in India. If it is considered difficult to deliver know-how to a representative of the Indian party in the foreign country, the foreigner may despatch the drawings etc, by post at the expense of the Indian party after taking instructions from the latter to this effect. The shipping company or the postal department, as the case may be, shall in this case, be regarded as agent of the Indian party and, thus, the delivery will be deemed to have taken place outside India.

It is important to emphasise that even though the delivery of know-how is made outside India, the payment by the foreigner must never be received in India. If this precaution is not observed, the profits on sale of know-how will be liable to tax on receipt basis, though not on accrual basis.

For securing services of technicians, the Indian party may enter into agreement with the foreign collaborator to supply suitable hands for executing erection work in India. It may be provided in the agreement that apart from the remuneration agreed to be paid to the foreign technicians by the Indian party, a lump sum shall be paid to the foreign collaborator for lending services of technicians. To support and justify this lump sum payment, it may further be provided that in case any of the technicians proves unfit for executing the erection contract in India, the foreign collaborator shall be liable to replace him by a suitable hand at his own expense. This procedure will enable successful completion of the erection work and at the same time save the foreign collaborator from Indian tax liability.

USE OF KNOW-HOW:

It is important to note that whereas the outright sale of know-how delivered outside India will not attract tax liability because no profits accrue or arise in India, yet if the know-how is intended for use in India, even though delivered in a foreign country, profits attributable to its use will be subject to Indian tax. At times, it is provided in collaboration agreements that the know-how after its use shall become the property of the seller and the Indian party shall be liable to return all the drawings, designs etc. to the foreign party so that the same might not be misused in India. This will be deemed to be a supply of know-how for use in India. To avoid this contingency, it is suggested that in foreign collaboration agreements a stipulation should be made to the effect that after its use the know-how shall be destroyed by the Indian party in the presence of an authorised representative of the foreign party to avoid its misuse in India.

INCOME FROM INTEREST ON MACHINERY SUPPLIED AT CREDIT:

Another form of collaboration may be the supply of machinery by a foreign party to an Indian party on credit at a prescribed rate of interest. In this case the interest will be exempt from tax under section 10(15)(iv)(c) of the Income-tax Act to the extent it is approved by the Indian Government. The Indian Government at present, as a matter of policy, does not approve interest at a rate exceeding 6% per annum. If, therefore, the interest agreed to be paid is 6% or below, the whole amount will be exempt from tax, otherwise the amount in excess of 6% will be taxable. To quote an instance, if the rate is 8%, only 2% will be subject to tax.

INCOME FROM DIVIDENDS:

In a financial collaboration, the foreign party may agree to invest in the share capital of the company formed in India for manufacturing purposes. The foreign party will be entitled to dividend on these shares as and when declared by the Indian company. The dividend shall be liable to Indian tax. If the foreign party is a company within the meaning of section 2(17) of the Income-tax Act, the rate of tax deductible at source will be only 25% and even 15% if payable by an Indian company referred to in the proviso to section 85A of the Income-tax Act. On the other hand, if the foreign party is not a company, it will be taxed as an association of persons in which case, the rate may exceed even 65% depending upon the amount of dividend. It is, there-

fore, advisable for a foreign party investing in the share capital of a company in India to have itself declared, if possible, as a company by the Central Board of Direct Taxes under section 2(17) of the Income-tax Act.

8. INCOME FROM ROYALTIES TECHNICAL FEES:

The rates for deduction of tax at source from non-resident companies on incomes arising from "royalties" and "technical fees" in India have been prescribed as under:

1. On Royalties:

(i) In the case of Agreements entered into on or after 1st April, 1961 – 50%

(ii) In the case of the Agreements entered into before 1st April, 1961 – 70%

2. On Technical Fees:

(1) in the case of Agreements entered into after 29th February, 1964 – 50%

(ii) In the case of Agreements entered into before 1st March, 1964 – 70%.

Distinction in rates of tax based on the time of factor agreements appears to be illogical. Imagine the case of two neighbouring manufacturing concerns in a foreign country having entered into industrial collaboration agreements with the same organization in India on different dates. How will they feel about paying tax at different rates on the same type of income, just for some flimsy reasons? It will be fair and reasonable to introduce uniform rates of tax for deduction at source from royalties and technical fees irrespective of the dates of agreements. This is important from another angle also namely, some of the pro-revenue Income-tax Authorities may be tempted to interpret payment of royalties as payment of technical fees in respect of agreements entered into between 1st April, 1961 and 29th February, 1964 to collect tax at 70% instead of 50%. To circumvent this situation too, it is necessary to prescribe uniform rates.

9. DOUBLE TAXATION AVOIDANCE AND RELIEF AGREEMENTS:

India has entered into agreements for avoidance of double taxation of income with the following ten countries:

Pakistan, Ceylon, Switzerland, Sweden, Denmark, Norway, Japan, Finland, Federal Republic of Germany, Austria and Greece.*)

In addition, agreements with the United States of America, France, UAR and Australia are under negotiation and may be concluded any time.

Agreements for relief from double taxation exist with the following countries:

Aden**), Kenya, Tanganyka, Uganda, Zanzibar, Ghana, Nigeria, Sierra Leone, Gambia and Mauritius.

The difference between agreements for avoidance of double taxation and agreements for double taxation relief is as under:

In the case of former, no tax on income earned in the other country is payable whereas in the case of the latter, tax has to be paid first in both the countries and then relief claimed for reimbursement of the excess tax paid in accordance with the terms of the agreement. The first type of agreements are definitely more beneficial.

The countries with which there is neither an agreement for avoidance of double taxation nor for relief from double taxation, section 91 of the Income-tax Act provides for unilateral relief to persons resident in India. Such relief is available on the doubly taxed income accruing or arising outside India, but not on the income which is deemed to accrue or arise in India. This means that a person resident in India has ultimately to pay tax on his foreign income at the higher of the two rates.

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*) See p. 359 of this issue.

**) See p. 366 of this issue.

In the case of agreements for avoidance of double taxation, it is provided in all of them that the industrial or commercial profits attributable to a "permanent establishment" of a foreign concern in India will be subject to tax. If there is no "permanent establishment", no tax liability will arise. The term "permanent establishment" is synonymous to "business connection" which has been discussed heretofore. It may be noted that only such profits are taxable as can be attributed to a "permanent establishment".

DR. ROCHMAT SOEMITRO S.H.*:

TAXATION IN INDONESIA

An Outline

INTRODUCTION AND HISTORY

A great deal of the tax legislation still in force in Indonesia for the time being, has its origin from the Dutch colonial period; some of them date from the earliest twentieth century. During the Japanese occupation all tax regulations, ordinances, decrees etc. were not abolished, but they were maintained to be valid, in order to prevent a judicial gap. Only the fiscal year has been altered from 1st January-31st December into April 1st till March 31st.

The Japanese occupation army, which was also entrusted with the running of the civil administration, has promulgated one new tax decree on Alien in 1942 known as the "Extraordinary War Tax" this kind of tax was meant as a special contribution of all foreigners residing in Indonesia to cover the Japanese war expenses.

On August 17, 1945, the Indonesian independence was proclaimed. To keep the order the newly established government proclaimed that all legislation, including tax regulations remained valid as far as they were not against the provision of the Indonesian constitution of 1945, or replaced by new ones (see the transitory provision of the 1945 constitution.)

We distinguish two different areas in Indonesia, since the proclamation of the independence. One area was under direct control of the restored Dutch government, more known under the name of Netherlands Indies Civil Administration (N.I.C.A.) and it covered the main cities in Indonesia like, Jacatra, Semarang, Bandung, Surabaya etc. These cities were handed over by the Allied Forces to the Dutch administration. The other area was under supervision of the Indonesian government.

In the first mentioned area all tax regulations, acts, ordinances, etc. of the former Dutch government were exercised again, except the Income Tax Act 1932, which was replaced by the Provisional Income Tax Act 1944, called the Transitional Tax (Overgangsbelasting) previously known under the name of War Tax (Oorlogsbelasting). This tax act was prepared by the Dutch Government in exile in Australia in 1942, when they must evacuate because of the Japanese invasion.

The in 1944 introduced transitional tax differs from the original Income Tax Act 1932, because the first was intentionally made simple, in view of its application. Because of the war a great number of the tax officials had to serve in the compulsory military service, so that the tax office missed a great deal of the capable and experienced officials. The simplified income tax act was meant to be carried out immediately after the rehabilitation of the Dutch government in Indonesia. It was really meant as a provisonal act that would be replaced by a better one, as soon as the situation would make it possible.

In the area under the administration and control of the Indonesian Government, with Jogja as its capital, all legislation was exer-

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cised which was in force during the Japanese occupation, almost the same as which was valid in the Dutch area, with some exception. In this region, from the beginning, the previous Dutch Income Tax Act 1932 was exercised, with a slight modification. Besides some new taxes have been promulgated by the Jogja Government, e.g. the radio tax and the reconstruction tax I.

By act nr. 4,1952 the United Republic of Indonesia has been formed with the result that all areas throughout Indonesia came under one and the same government. The following taxes were declared to come into force for the whole area of the Republic of Indonesia as from January 1st 1951, viz:

1. Radio tax, promulgated in 1947 by the Republic of Indonesia,
2. Reconstruction tax 1, ibid,
3. Turnover tax, introduced by the United States of Republic Indonesia in 1950,
4. Transitional tax 1944, (a provisional income tax) promulgated by the Dutch government in 1944,
5. Wages tax, issued by the Dutch colonial government in 1935,
6. Household tax (personal tax) enacted by the Dutch colonial government in 1908,
7. Motor Vehicle Tax, introduced in 1934 by the Dutch government,
8. Transfer duties on immovables, introduced by the Dutch government in 1924,
9. Tax on slaughter of livestock, instituted by an order in 1936 by the Dutch government,
10. Stamp duties, dated from 1817 and renewed by the Stamp Duty Decree of 1921,
11. Death duties of 1901, instituted by the Colonial government,
12. Property Tax, instituted in 1934 by the Dutch government (for description of the respective taxes see later)

Taxes mentioned under nr 1 and 2 originated from the Jogja Government, while the Turnover Tax was enacted by the United States of Republic Indonesia in 1950. The Transitional Tax 1944, as mentioned before, was prepared by the Dutch Government in evacuation. The remaining ones dated from the Dutch Colonial Administration before 1942.

It was not clear yet and it has not been possible for me to obtain any information on the reason why the Company Tax was not mentioned in the above discussed Act (Act nr. 4,1952) although the Company Tax has never been abolished but was continuously exercised in Indonesia.

Since 1952 several new taxes and legislation on taxes have been promulgated, viz:

1. Purchase Tax 1951; this is to replace the Turnover Tax 1950 mentioned before,
2. Dividend Tax 1959,
3. Alien Tax 1958,
4. Tax on Income derived from Agriculture, 1959,
5. Tax Collection Act 1959,
6. Transfer Tax on Motor vehicles 1959,
7. Compulsory Contribution on Buildings 1962,
8. Compulsory Contribution on Motor Vehicles 1962,
9. Compulsory Contribution on Radio 1964,
10. Compulsory Contribution on Luxury Goods 1964.

ORGANIZATION OF THE INLAND REVENUE ADMINISTRATION

Before dealing in details with the respective taxes it is worth while mentioning briefly the organization of the Inland Revenue. The Inland Revenue Department, side by side with the Custom and Excise Department, is constituted as a part of the Ministry of Fi-

nance, more known as the Directorate General of Inland Revenue, and is headed by the Director General of Inland Revenue. We distinguish in the Directorate General of Inland Revenue:

a) the Administration Division, which is divided into:
i. general services and personnel department,
ii. central administration (processing data for the preparation of the budget, supervision of the tax collection and other administrative work),
iii. information and field service division.
b) the technical division, which is divided into:
i. directorate of direct taxes, which administers and controls direct taxes,
ii. directorate of indirect taxes, which administers and controls indirect taxes (issuing of circulars, interpretation, investigation of complaints and appeal cases, planning tax act etc.).

The Inland Revenue Department is responsible for the imposition and collection of all taxes, both direct and indirect taxes, except custom and excise duties. The whole area of Indonesia is divided into 35 tax districts, each consisting of:

a Central administration division;
b Execution of tax legislation division (assessments);
c Field service division;
d Tax collection division.

The tax Accounting department, formerly a division of the State Accounting service, has been separated from it recently and became a part of the Directorate General of Inland Revenue.

TAX LAW AND LEGISLATION

Article 23 bis of the 1945 Constitution, provides that: "No taxes for the benefit of the Treasury can be imposed on the people except by law". Furthermore article 16 and 17 of the Indonesian Treasury Act (Indische Comptabiliteitswet) laid down the principle, that all legislation intending to impose, to increase, to reduce or to abolish taxes, will not come into force than after the sum resulted from it has been taken in consideration in the annual budget and that no taxes shall be refunded or annuled except by law or under such conditions as law may prescribe.

In order to implement the tax law, the Minister of Finance can enact ministerial orders. Also the Director General of the Director of the Inland Revenue can issue directives to officials of the Tax Administration and to its local offices for the uniform interpretation and application of laws and ordinances.

NATIONAL TAX AND LOCAL TAX

Based on the principle of local autonomy, as set forth in the Basic Act for Local Government local public entities shall have the right to manage their own property, affairs and administration and to enact their own regulations within law.

They can assess and collect taxes as provided by law. On these provision local public entities are given the right to assess and collect local taxes. The range of field that can be covered by the local tax is what has not been covered by the national tax, like admission tax on public performances, tax on vehicles other than motor vehicles, tax on buildings situated in the main street, business licences etc.

By act nr. 32,1956 a number of national taxes viz. the Landtax, tax on motor vehicles, Household tax (Personal tax), Copra tax, Road tax, Slaughter tax on livestock, Reconstruction tax I, has been transferred to local public administration, as from January

1957. From some other taxes only a part of the yield has been put at the disposal of local entities. In this context can be mentioned the Income Tax, Wages Tax (abolished since 1961), Stamp duties, property tax and the Company (Corporation) tax.

TAXES ON INCOME

A. INCOME TAX

The Income Tax Act at present in operation in Indonesia is the Transitional Tax Act 1944, which has been drafted by the Dutch Government in Australia. The series of amendments and modifications made to the original text, have hardly affected its structure.

The Income Tax is imposed on the individuals' income, while the Corporation Tax (or Company Tax) is imposed on Corporations' income. With regard to the accounting period the individual taxable income, unlike the corporation income, is computed on the calendar year basis. In other words the accounting period for the individual income concerns from January 1st through December 31st of the year.

TAXPAYERS

The taxpayers of Income Tax are classified into "taxpayers resident" and "taxpayers nonresident." An individual is classified as resident taxpayer if he has a domicile in Indonesia, or if he intends to reside in Indonesia whether or not permanently. Also those who have no intention residing in Indonesia permanently if they have been residing in Indonesia for 12 months or more.

An individual domiciled or resident in Indonesia must pay Income Tax on all his income derived from sources within Indonesia as well as from sources from abroad, as provided in the Income Tax Act. These sources can be classified as follows:

i. enterprise and labour; f.i. business income and earned income;
ii. real estate;
iii. capital used other than for enterprises, such as dividend, or interest;
iv. periodical allowances (retirement income, allowances paid to divorced wives).

A nonresident individual means any individual other than resident.

A taxpayer nonresident is only subject to income tax on his total income derived from sources within Indonesia, under the following circumstances:

i. he derives income from immovables located in Indonesia;
ii. he receives payment or renumeration for his personal services rendered in Indonesia, or from carrying business in Indonesia either by himself or by his representative;
iii. he receives interest on loan which is secured by a mortgage on immovables located in Indonesia;
iv. he receives any payment other than mentioned under ii from business in Indonesia, such as royalties for the use of copyright, patent and other like property;
v. he receives salary, pension and other payment for his services on account of the enterprises in Indonesia.

The income to be taxed is the individual income of the current year. As the year income can only be composed when the year is expired, the taxpayer has to file the return after the end of the current year.

TAX RETURN

Who is required to file a return?

Anybody who receives a return form from the Inland Revenue, has the duty to file the

return within 30 days (normally) notwithstanding his income is below the minimum taxable income, either he has no income. Besides anybody who has an annual income which is above the minimum taxable is required to file a return although no return form has been sent to him. Those who failed to file the return or who neglected his duty will be subject to administrative punishment.

TAX BY ASSESSMENT

As a rule the income tax is levied by assessment in the year following the current year, but considering the pressing needs of the State Treasury, during the course of the current year, the system of provisional assessment is applied. This is based on income actually enjoyed during the preceding year. The provisional assessment will be followed by the final assessment, which could be higher, lower or the same as the provisional assessment. In case an individual deemed liable to file a return, has failed to file it, the tax authority shall on its own investigation determine the amount of his income on an estimated basis and at the same time add the penalty amount of 25% of the tax amount due.

TAX PAYMENT

The taxpayer is required to pay the amount of tax as follows:

a) for the temporary tax assessment, in so many equal instalments as the number of months of the calender year is left after the month in which the assessment notice has been issued. Every payment is due on the fifteenth of each month.

If the temporary assessment notice has been issued after July 31 of the current year, the tax is payable in 5 equal instalments, starting from the month following the month of issue;

b) for the final (definitive) tax assessment, the whole amount must be paid within three months, at latest by the 15th day of the 3rd month following the month in which the notice of assessment has been issued.

TAX BY WITHHOLDING

Those who pay salaries, wages (employment income), royalties, renumerations specified by the Income Tax Act, are required to withhold income tax and shall pay the income tax so withheld to the Treasury not later than the 15th day of the month following the month during which the withholding has taken place. The tax authority shall issue a notice of payment to those who neglected the withholding or failed to pay the tax so withheld. The withholding must be exercised according to the tax rates and in a manner as prescribed by the regulations laid down in the "Guidance for employers to withhold Income Tax". If an employee does not derive any income from other sources than salary or wages, he will not be assessed by way of an assessment, but the income tax withheld by the employer will be the final tax. But if the taxpayer has income from other sources than salary or wages, say from immovables, business etc, the tax authority will issue an assessment on the aggregate income enjoyed by the taxpayer. The tax withheld is in effect a prepayment of the income tax and will be credited against the taxpayer's final liability of the year.

In order to make the withholding of income properly, the recipient of salary or wages has the duty to submit to the employer a statement concerning the exemption of dependents.

As to monthly paid salary, the tax amount is fixed by the "monthly tax table" according to the amount of salary paid and the number of dependents.

As to weekly paid wages, before applying the monthly tax table, the amount must be multiplied by 4.

As to daily paid wages, consisting of more

than 4 working hours the amount must be multiplied by 26.
Daily wages for not more than 4 working hours, must be multiplied by 52.
Before the abolishment of the Wages Tax, beginning from January 1, 1961, wages tax must be withheld from all kind of payments done by an employer for services rendered.
The withholding system in Indonesia is to be compared with the "Pay as you earn" system in Great Britain and the "Pay as you go" system in the United States of America.

COMPUTATION OF INCOME

The taxable income is computed by adding all the net receipts derived from the sources as mentioned above. By net receipt is meant the gross receipt of any sources after having been deducted by the necessary expenses (see below)
The sum of the net receipts of the sources forms the gross income of the individual. If we deduct the personal charges from the gross income we get the net income. The taxable income is then the net income deducted by the personal allowances.
The amount of receipt is determined in principle when the amount to be received is determined, this is the so called "accrual basis". Not only the money received, but also the value of other properties and services rendered must be evaluated and included in the income, such as payment in natura (rice, sugar, textile etc), free housing, free motor vehicle etc.
The necessary expenses mean the expenses that are deemed necessary to acquire the receipt of the year. The necessary expenses varies with the kind of income source (see below). So the net income is the remainder after deducting the personal charges from the gross income. The taxable income is the annual net income deducted by the personal allowances.

Deemed as necessary expenses:

A. Income on business:
1. the cost incurred in securing, collecting and preserving proceeds income and the charges connected with the proceeds, (cost of the sales of merchandise);
2. the amount of depreciation of property used in a profession or business;
3. rentals for buildings and land used for business;
4. fire insurance payment;
5. tax and duties on properties used for business;
6. wages, salaries etc. for employees;
7. expenses for water, light, telephone, gas;
8. expenses for social purposes (limited);
9. interest paid on business indebtedness;
10. writing off bad debts;
11. the compulsory contribution for pension and pension funds connected with salaries and other allowances including leave pay, subsidies, unemployment payments, pension and annuities;

B. Income from immovables:
1. maintenance expenses;
2. premium for fire insurance;
3. expense for collecting;
4. tax and duties on immovables;

C. Income from movables, and capital other than which is used in enterprises like dividend, interest:
1. expenses for collection;
2. insurance premium;
3. expenses for maintenance;
4. expenses for storing.

D. Income from periodical allowances:
1. expenses for collection

PERSONAL CHARGES

By this we mean, that charges with personal character is deductible viz:
a) personal allowances paid to divorced wives based on judicial sentence;
b) interest paid for personal indebtedness;

c) premium for life insurance and pension other than the compulsory premium as mentioned above;
d) pension paid to ex-personal employees.
But from January 1, 1966, premium for insurance and pension are not allowed to be deducted any more by reason that the personal allowances (infra) are deemed to be enough to cover such expenses.

PERSONAL ALLOWANCES

MINIMUM TAXABLE INCOME

Before applying the tax rate the income of the resident taxpayer is to be deducted by the personal allowances as follows:

	monthly	yearly
a) for the taxpayer himself	Rp 175,—	Rp 2.100,—
b) for the legitimate wife (wives) each	Rp 100,—	Rp 1.200,—
c) for every dependants to a maximum of 10 persons each	Rp 50,—	Rp 600,—

These amounts personal allowances constitute the minimum taxable income.
A person, married, with 2 children will not be liable to income tax if he earns yearly not more than Rp 4.500,—
From January 1, 1967, this minimum is multiplied by 4.So in the above mentioned case the taxpayer is not subject to income tax if his annual income amounts not more than Rp 18.000 or his monthly income is not exceeding Rp 1.500,—
Since the tax authority allowed personal allowances to the taxpayer himself and to his legitimate wife (or wives) and dependants as mentioned above the deduction of premium for social insurance or pension has been abolished. It is deemed that social expenses could be covered by the deductible amount.

THE SELF-ASSESSMENT SYSTEM

Until 1966 the self-assessment system has not been applied in Indonesia, but from January 1, 1966 the Indonesian tax authority has tried to apply this system.
Every tax payer running business is recommended to pay the tax on basis of self assessment.
A special tax return form has been drafted and distributed to the taxpayer in order to enlighten and to encourage every taxpayer to calculate himself the income tax due. To my opinion the situation and the educational level of the average taxpayer in Indonesia is for the moment not suitable for applying the self-assessment system. If a self-assessment system is to be succesful, the condition of a severe tax discipline must be first fulfilled. It could be tried as a pilot project to a certain group of taxpayers, who are deemed to have the capacity and the ability to compute and to calculate their incomes. During two years of experiment the self-assessment system does not give any satisfaction Maybe in the near future, if the conditions will be favourable, the self-assessment system will give more hope.

TAX ON INCOME BELOW RP 18.000 (TILL 1965)

This group of taxpayers, most of them self-employed workers, does not have to submit income tax returns. They are taxed at a flat rate, under a classification system, based on external signs of prosperity. A regional commission, whose chairman is an official of the Ministry of Internal Affairs, and whose members are appointed by the Regional Officer (Regent) enters in a special session, noting the class of income bracket to which each taxpayer belongs. The chief Revenue Inspector is entitled to attend or to be represented at the meetings of the commission, but in a purely advisory capacity. The district officer of the Ministry of Internal Affairs functions as the district revenue officer and is responsible for the collection of

the taxes. This provision has been abolished since January 1, 1965. From that moment self-employed workers with an income above the taxable minimum, will be assessed in the ordinary way, as all other taxpayers without any distinction.

Tax Rate (in operation since January 1, 1966)
Income which exceeds the minimum taxable income are taxed as follows:

Taxable Income (after deduction of personal allowances)	*Basic tax*	*Additional rate* for each full Rp 100,—
Rp 0	Rp 0	Rp 21,—
Rp 4.800,—	Rp 1.008,—	Rp 27,—
Rp 11.200,—	Rp 2.736,—	Rp 36,—
Rp 24.000,—	Rp 7.344,—	Rp 45,—
Rp 120.000,—	Rp 50.544,—	Rp 54,—
Rp 240.000,—	Rp 115.344,—	Rp 60,—

Tax rate, applicable to employees (other than partners in a partnership)

Taxable income (after deduction of personal allowances	*Basic tax*	*Additional rate* for each full Rp 100,—
Rp 0,—	Rp 0,—	Rp 21,—
Rp 12.000,—	Rp 2.520,—	Rp 27,—
Rp 24.000,—	Rp 5.760,—	Rp 36,—
Rp 72.000,—	Rp 23.040,—	Rp 45,—
Rp 240.000,—	Rp 98.640,—	Rp 50,—

Compared with the earlier mentioned rate, this rate is more moderate. Rate "A" which is meant for self-employed workers with an annual income not higher than Rp 18.000,— and rate "C" which is meant for nonresident taxpayers have been abolished respectively by Governmental decree no 53 and by ministerial decree Nr. P.Pd 1-5-16/1964.

RATE FOR CASUAL WORKERS

For casual workers the following rate is applicable:

Daily wages Rp 0,— up to Rp 10,— : 0%
Rp 10,— up to Rp 14,— : 3%
Rp 14,— up to Rp 20,— : 5%

If the daily wages amounts more than Rp 20,— the second rate mentioned above will be applied.

RATE FOR ROYALTIES, RENUMERATION PAID TO AUTHORS, ARTISTS, PRIVATE TEACHERS, ADVISORS ETC.

A flat rate of 5% is withheld to all kinds of payments as a prepayment of the income tax assessed. The amount withheld will be credited against the income tax.

SPECIAL RATE APPLYING TO CERTAIN EXTRAORDINARY PROFITS AND CAPITAL GAINS

Profits derived from the transfer, winding up or liquidation of a business or from property, other than merchandise, and money received in lieu of income or in compensation for the non-execution of any transaction or for relinquishing the right to share in the profits of a business or other gainful activity, are taxed at a flat rate of 10%. This kind of profit is computed quite apart from the ordinary income.

Since January 1966, profits derived from the transfer of personal property, either movable or immovables, are also subject to this special rate.

In case the transferred commodity is an immovable the profit enjoyed will be only subject to income tax if the price of the immovable concerned exceeds Rp 100.000,— or if the commodity has been owned for less than 12 months after the date of purchase.
In case the transferred commodity is a movable the above mentioned limit becomes Rp 25.000 or 6 months.
In both cases no tax is imposed if the origin of the commodity is an inheritance or a gift.

TAX CREDIT

Taxes, withheld at the source, except dividend tax, such as income tax on employment income, retirement income, royalties etc, which are deemed to be an advance payment of the income tax, are credited against the income tax assessed.

Dividend tax is withheld at a rate of 20% from dividend and all kind of payments which are actually profit distribution. Dividend tax, previously deemed as a prepayment of income tax, is credited against income tax, but since January 1966 this provision has been amended. Now dividend tax has become a final collection and cannot be credited against income tax, because the dividend enjoyed does not constitute a part of the income.

Foreign income tax is also credited against national income tax. If a resident taxpayer pays income tax on income derived from sources abroad, the foreign income tax is credited against the national income tax assessed. Not the amount of foreign tax actually paid is credited, but the amount of national income tax which is based and computed according to the ordinary Indonesian rate. In this case the ordinary rate is applied to the income enjoyed abroad.

TAX ACCOUNTS

Every taxpayer who runs business is obliged to keep regular accounts if within one of the years preceding the current year his turnover exceeds a certain amount. The obligatory accounts are also meant to be observed by taxpayers who are appointed by the tax authority to do so.

The accounts must be adequate and must be exercised in a way so that any obligation against third parties could be traced at any moment.

At the end of the fiscal year the taxpayer has to produce a balance sheet which shows the amount of profit enjoyed. The balance sheet must be attached to the tax return. The accounting must be done according the provision laid down in the income tax act. Taxpayers having the obligation to keep regular accounts, but who fail to do so, are subject to administrative penalties which appear as an additional amount to the tax assessed. The qualified tax officers have the authority to evaluate the balance sheet and to amend or to refuse the figures of the balance sheet if they bear the suspicion that the accounts are not reliable or are not based on true facts, even if the balance sheet has been composed by a public accountant.

This is quite different from the practise in Great Britain and the U.S.A. where the financial report of a C.P.A. is accepted for correct, except if there is a strong evidence of malversations.

DEPRECIATION

Depreciation for computing the taxable income is only allowed to individual enterprises which keep regular accounts. Subject to depreciation are tangible fixed assets, such as machineries, equipment or buildings and intangible fixed assets, such as copyright, patentsright of business, deferred expenses used in enterprises. There are no apart depreciation rules for income tax, but the depreciation rules for the company tax (corporation tax) as laid down in the Depreciation Order 1953 are applied for computing the taxable profit in income tax, although with some exceptions.

Depreciation is based on the acquisition costs or residual value while the replacement value is not allowed.

The useful lives of fixed assets is legally determined by ministerial order. A few examples of which are given below:[1])

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1) The complete list is reproduced infra: Company Tax, depreciation.

Facilities	Useful life (years)
Permanent buildings	15-40
Agrarian plants	16-25
Industry	8-12
Water transport equipment	10-12
Inventory	5-10

The category to which an item is assigned and the period of depreciation may not be changed, once they have been decided on by the taxpayer. The normal system applied is the straightline depreciation. The free depreciation, immediate depreciation and the accelerated depreciation is not applicable in income tax (see about this under the company tax)
Bad debts may be written of.

NON TAXABLE INCOME

Non taxable income is defined in the provision of the Income Tax Act. Some of the principal items are:

a) The enjoyment of free housing of the President of the Republic of Indonesia;
b) Livelihood allowances (alimony) received from dependants;
c) Enjoyment of free medicine and medical treatment;
d) Enjoyment of free housing and food of ship's personnel;
e) Enjoyment of free housing in the barracks of the military personnel;
f) Compensation for travel expenses;
g) War allowances paid to military personnel.

PERSONAL EXEMPTION

Exempted from income tax are representatives of foreign countries, ambassadors, consuls, etc. on condition laid down in the Income Tax Act.
Those persons are not liable to income tax, according article 9 of the Act, if they are not Indonesian citizens, and they do not derive any income from undertakings in Indonesia; besides, the tax exemption depends on the reciprocity principle, that means that Indonesia will grant a tax exemption, if that country does the same to Indonesian representatives. This tax exemption is not based on a mutual agreement but on international custom and courtesy, although in 1961 the Vienna Convention on diplomatic immunity has been signed, of which Indonesia is one of the participants.
Furthermore are exempted representatives of foreign international organizations, military attaches as the law may prescribe.

PROFIT OF PARTNERSHIP

Before the Income Tax Act has been amended (beginning January 1966) partners of partnership are subject to Income tax for their shares in the profit. After the modification the whole profit of the partnership is liable to Company tax, and if the profit is distributed to the partners, dividend tax will be levied on the profit distributed. In this case no income tax will be imposed on the partners, because the dividend tax withheld at the source by the partnership forms a final levy. It is obvious that the profit enjoyed by the taxpayer does not constitute a part of the income of the taxpayer.
By the "whole profit" as mentioned above we mean the net profit of the partnership after deduction of a certain amount, which is deemed to be sufficient to pay the salary and gratification of the partners. This amount will be fixed annually by the Minister of Finance and will take the form of a fixed percentage of the net profit.
Practically this amount is considered as an expense which is deductible from the gross profit. So this amount is not liable to company tax or income tax as well.
If the amount exceeds the limits, the excess amount is subject to the dividend tax.

TAX DISPUTES

A taxpayer may enter a claim with the district revenue officer under whose jurisdiction his assessment was drawn up. If he is not satisfied with the assessment, a request of reconsideration may be made to the chief of the district revenue office.

The District officer is required to take a decision on that request.

Those who have an objection against any decision of the district revenue officer concerning his request may appeal to the Appeal Board in Djakarta for remedy, within three months after the decision has been made. In the tax litigation, the plaintiff is the taxpayer and the defendant is the tax authority.

The litigation is exercised in accordance with the normal procedure applicable to the ordinary civil trial and the decision of the Board of Appeal on the dispute will be binding, not only to the related parties but also the executive branch as a whole.

The Board of Appeal is instituted in 1927 and deals with appeals of direct taxation as the provision of the appropriate law may prescribe.

Besides the Board of Appeal, the ordinary court has the power to take into consideration queries and appeals in the field of indirect tax.

TAX COLLECTION

The provisions set forth hereafter have a general character, that is to say that they are applicable to direct taxes and indirect taxes as well.

National taxes are collected in accordance with the Tax Collection Act, which is enacted in 1959. This act provides the rules of the tax collection.

To secure a sound and easy collection the following provisions are made:

a) Priority is given to tax liabilities against private claims.

Priority to tax claims can only be given up against those creditors secured with the right of mortgage created upon the taxpayer's immovables before the notice of assessment. Priority is not given to the right of pledge.

b) When a taxpayer fails to pay tax in full by the due date, the district revenue officer having jurisdiction over the area where the taxpayer lives, sends a note of demand. If the taxpayer has not paid off the due tax within the time-limit mentioned in the notice of demand the tax authority shall attach the taxpayer's properties. Attached properties are sold in principle by public sales.

The tax authority shall give public notice of the properties to be sold at least 2 weeks before the date of sale, and he also shall notify the delinquent taxpayer and other related parties. The public sale is made by auction. The proceeds of the properties sold are appropriated in order of priority, among the delinquent taxes, for which the properties were attached, and other public charges for which request for share distribution has been made. The remainder, if any, will be delivered to the delinquent taxpayer.

If the taxpayer has no properties to be seized and if he is unwilling to give contributions to the tax authority, the taxpayer could be imprisoned for debt on request of the tax authority.

c) If a taxpayer is in arrear for more than two instalments, a note of demand to pay the whole tax amount will be sent to him.

d) In case of liquidation, or if the taxpayer is going to reduce the size of his undertakings or if he is going to alienate his properties, so that the due payment of the tax is endangered the tax authority is entitled to collect without delay the tax of the taxpayer whose due date of payment has not yet come.

e) Taxpayers who are going abroad are required to pay the tax due, in order to obtain a tax clearance certificate.

f) Taxpayers who fail to pay by the due date, must pay an interest of 5% of the delayed payment.

TAX PENALTIES

According to the social justice and in order to attain the tax equity, the correct tax return should be filed and the due collection of the payment of the tax should be made in accordance with the tax laws.

To attain the above mentioned purpose, penalties are provided in both the administrative and judicial respect, in case the obligations prescribed in the tax law are defaulted by the taxpayer without reasonable excuse, such as if he neglects to file the tax return or if he makes incorrect tax return by omitting any taxable income.

A default of obligations such as a failure in filing a tax return or a filing of a tax return which is not based on true facts is punished by an administrative penalty.

The judicial penalty is to be imposed upon the tax crime in connection with the assessment and collection of tax, and the necessary condition to penalize as well as the content of penalties are stipulated in the respective tax law.

B. COMPANY TAX

Company tax or Corporation tax is actually a tax on income enjoyed by nonindividuals. The Company Tax Law now in force is based on a Netherlands Ordinance of 1925, amended by a series of later enactments. Subject to this tax are domestic companies, as well as foreign companies.

A domestic company means a company settled in Indonesia and established on the basis of Indonesian Law. A foreign company means a company which is not settled in Indonesia.

Obligation to pay Company Tax extends not only to Corporations (such as limited companies, joint stock companies, limited partnerships) but also to juridical persons (foundations, organisations with juridical status) and even to associations without juridical personality on conditions laid down in the Company Tax Act.

Corporations, whose capital is divided into shares, are liable to company tax for the whole profit derived from capital used within undertakings, as well as capital used outside the undertakings.

Associations and juridical entities in public interest are subject to company tax, only for the income derived from profit-making business activities, while they are subject to either Income Tax or Company Tax on such income derived from assets, as interest on deposits, dividends or income from real property etc.

A foreign company is subject to Company tax on condition that:

a) it derives income from immovables situated within Indonesia;
b) it has enterprises which are operated in Indonesia by a permanent establishment which has its domicile in Indonesia;
c) it has claims used outside the enterprise which are secured by a mortgage on immovables located in Indonesia;

Foreign companies are regarded as carrying on business within Indonesia, when they carry on business in a fixed place by a Permanent Establishment. In the absence of any legal definition, a foreign company is deemed to have a permanent establishment in Indonesia if it has a permanent installation (e.g. branch, office or factory) in Indonesia, or a permanent representative with full power to enter into contracts on its behalf.

Not considered as carrying on a business in Indonesia by foreign companies are:
transports by sea or by air of persons and goods between ports or airports located within and outside Indonesia by foreign ships or aircraft, on the condition that in the foreign country concerned a reciprocal exemption of tax is granted for profits obtained from international shipping traffic by ships sailing under Indonesian flag, or from profit obtained from international air traffic with aircraft employed by companies which have their domicile in Indonesia.

NON TAXABLE CORPORATIONS

Among the corporations to be exempt from the Company tax are the State enterprises carried on by Government agencies, according to the provisions as set forth in the Indonesian Treasury Act (I.C.W.)
However, enterprises owned by the State which are carried on by limited Companies such as the Railways, the Post Office service, electricity etc. are liable to Company Tax. Cooperative bodies, composed according to the cooperative bodies Act, are exempt from Company Tax for 5 years following their establishment. Up till 1965 new emerging national enterprises, over a period of 5 years following its establishment will be taxed according a special rate, which is much lower than the ordinary rate. As from January 1966 this rate is abandoned.

PROFIT/TAXABLE INCOME

The term "profit" according to article 3 (1) and (2) means the net sum of benefits which in any amount or from whatsoever are derived from an undertaking or from capital otherwise invested. These benefits include those resulting from the alienation of property not intended for sale and in general any benefits derived from such property even after the undertaking has ceased its operations.
Profit in this sense must be interpreted as the profit which is not influenced by the taxpayer's opinion or by the method of entering the accounts, but it is merely based on true and reasonable facts.
The Company tax is imposed on income enjoyed during the accounting year, unlike the income tax on individuals which is based on the calender year. According to the provisions of the Commercial Law and the Fiscal Law, corporations, juridical persons, associations who are subject of the Company Tax, are required to keep accounts and records.
The tax base of the Company tax consists of the ordinary income or the liquidation income. To the ordinary profit is applicable the ordinary rate (see infra).
Distiction must also be made between profits received from the alienation of property not intended for sale such as non-merchandise e.g. machines, buildings etc. and profits which are the result of liquidation, because they are treated differently.
Profits received from the alienation of property not intended for sale are taxed at a flat rate of 10% if that property has been owned by the corporation for more than 4 years. Otherwise the ordinary rate is applicable. (article 10a Company Tax Act)
When a corporation ceases to exist, either by dissolution or by merger, the company tax is charged on its liquidation income. There are two possibilities to tax the liquidation profit:
A. Provisions are valid till January 1966.
1. Liquidation profits are treated in the same way as the ordinary profits, to which is applicable the ordinary rate.(art.3)
2. Liquidation profits which fulfill the provisions of article 3 par. 4 of the Company Tax Act, on request of the taxpayer, could be exempted from the tax on conditions that the levy of the tax on the profit concerned is secured in the future.

B. Provisions which are valid as from January 1966.

1. Liquidation profits are taxed at a flat rate of 10% (art. 10a). From this must be excluded the benefits resulting from the sale of merchandise.
2. Liquidation profits are exempted from the Company tax on the same conditions as mentioned under A.2.

THE COMPUTATION OF THE INCOME/PROFIT

To calculate the corporate income, the gross revenue must be deducted by the allowable expenses and depreciation.

Deductible expenses are:

(a) The costs incurred in securing, collecting and preserving proceeds income and the charges connected with the proceeds, viz:

1. cost of raw material needed,
2. labour cost needed,
3. packing/wrapping costs,
4. storage cost,
5. cost for services rendered by third parties,
6. cost for transportation of the goods/product,
7. distribution cost,
8. overhead cost,
9. cost for electricity,
10. interest on loans,
11. advertisements cost,
12. collection cost,
13. insurance premium,
14. indirect tax on goods such as purchase tax, stamp duties, motor vehicle tax etc.,
15. royalties paid to employees/authors,
16. direct taxes, viz: income tax of employees paid by the company, household tax, landtax,
17. charity contributions, limited to 3% of the taxable income, etc.

(b) Depreciation.

Deduction of wear and tear and depreciation for the purpose of ascertaining the net profits chargeable with Company tax shall be in accordance with the Depreciation order 1953. (see later)

NON DEDUCTIBLE EXPENSES

According to article 5 of the Company Tax Act (C.T.A.) in computing the costs, the following items are excluded from expenses for tax purposes:

(a) expenditure for the purchase, repair (improvement) or alteration of land, buildings, instruments and other articles used in undertakings, except if those expenses are deemed as ordinary daily expenses;

(b) expenses to take over, or expenses for the expansion, improvement or alteration of an undertaking and other expenditure of that kind;

(c) the formation of a reserve fund of any kind;

(d) interest of own capital;

(e) interest or compensation paid, directly or indirectly for the use of articles submitted by persons or corporations, who are entitled for more than 50% to the subscribed capital;

(f) taxes levied in Indonesia on profits or any kind of taxes levied abroad on profits enjoyed in Indonesia;

(g) any kind of payments out of the profit to any person or corporate bodies except shareholders (for instance dividends or bonusses paid to shareholders) indebted or not, except payments done to the State, and payments to other people than commissioners, delegates, directors, for their services rendered. Directors' remunerations or retirement allowances are as a rule deductible if these do not exceed the reasonable basis or the amounts as set forth in the articles of incorporation or as decided by the stockholders' general meeting.

DEPRECIATION

The basic provisions on depreciation laid

down in article 4 C.T.A. can be summarized as follows:
(a) Initial expenses and costs for expansion of the capital can be depreciated freely according to the accounts;
(b) Capital expenses and deferred expenses, such as experimental research expenses may be depreciated according to their useful lives, as the regulations of the Minister of Finance may prescribe;
(c) Investments which fit in the Government's program on Indonesian prosperity are subject to a special depreciation as prescribed by the Minister of Finance (see later art. 9);
(d) The durable decline of capital participation and bad debts can be written off according trade custom;
(e) The profit received from capital used outside the undertaking may be deducted by the amount of writing off on rights with limited lives.

The method of depreciation prescribed by the Depreciation Order 1953, is the straight line method. The declining balance method and the replacement method are not used. The basis of the depreciation is the acquisition cost and the statutory useful lives or the number of years during which such expenses are serviceable. The acquisition costs of fixed assets which provide the basis for computing the depreciation charges are the purchase prices in case the fixed asset has been bought from others; the market price in case of fixed asset acquired as a gift or trade-in, and the total costs of raw materials, labour costs and other necessary expenses in case the fixed asset has been constructed or manufactured by the corporation itself.
Depreciation allowances shall be computed in principle for individual items or groups of properties. The category to which an item is assigned and the period of depreciation may not be changed, once they have been decided on by the taxpayer. Sale or alienation of the item does not alter the course of depreciation, except at the request of the taxpayer to write off in one operation the undepreciated balance in the year of sale. If the item belongs to a group of property of which the individual undepreciated balance is not known, the amount of sale received may be added to the normal depreciation of the items of the group in the year concerned, and the remaining undepreciated balance of this group may then be distributed over the number of years that still remains. The amount of sale received forms a part of the assessable profit. The total of the yields of the sale and the annual depreciation may not exceed the amount of the undepreciated balance.
The useful lives of fixed assets are legally determined by the provision of article 4 of the lately amended ministerial Order.

Facilities	Useful life (years)
I. 1. Buildings.	
A. Buildings, not being a dwelling or resthouse used in the agricultural, industrial, mining or transportation field	
(a) permanent buildings	15 till 40
(b) semi permanent buildings	10 till 15
(c) wooden buildings	8 till 12
B. Buildings, not being a dwelling or resthouse used in undertakings, other than mentioned under A,	
(a) permanent buildings	40 till 50
(b) semi permanent buildings	15 till 40
(c) wooden buildings	10 till 15
C. Dwelling	
(a) permanent dwellings	50 till 75
(b) semi permanent dwellings	20 till 40
(c) wooden dwellings	10 till 15
2. Inventory (included typewriters, calculating machines) etc..	5 till 10
3. Land transport vehicles, included tractors etc	5 till 10

4. Water transport vehicles, included docks etc.	10 till 12
5. Airplanes,	7 till 10
6. Motor vehicles and luxurious station wagen used by taxi cab companies for public transport	5 till 10
7. Deferred expenses if the useful life could be determined exactly	the useful life
8. ibid if the useful life could not be determined exactly	5 till 10

II. Expenses spent on equipment of undertaking not mentioned under nr. I, used
(a) in the agrarian sector (included farming and fishery) 16 till 25
(b) in industry, mining and transport sector 8 till 12

III. Expenses for luxurious inventory and resthouses are not allowed for depreciation.

INVESTMENT

Investments which fit in the Government's program on Indonesian prosperity are depreciated according to a special provision laid down in article 9 of the amended Ministerial Order 1953. This provision is only applicable on request of the taxpayer and subject to this depreciation are investments, which increase directly the production of goods, exercised by Indonesian enterprises in the field of agriculture, industry, mining and transportation, except expenses for equipment previously already in operation in Indonesia and expenses of a luxurious character.

The expenses may be freely depreciated over a period of four years from the date on which it was incurred or from any other date selected by the company. If there is an undepreciated amount left after the expiration of the 4 years' period, this amount is to be depreciated according to the provision of article 4 of the Ministerial Depreciation Order.

Expenditures for plain housing of employees are treated equally. The original article 9 of the Depreciation Order has been abolished as from June 1959, but afterward re-enacted and become valid again as from June 1961 with some modification.

TAX RATE

There are three different rates in the C.T.A.

A. The ordinary rate;

B. The rate applied to newly established companies, corporate bodies, co-operative bodies etc;

C. The rate applied to profits received from the alienation of property not intended for sale and liquidation profits.

A. The ordinary rate is laid down in article 10 of the C.T.A.

Taxable profit					Tax liability
		not over	Rp	500.000,—	40%
over Rp	500.000,—	but not over	Rp	1.000.000,—	42,5%
,,	Rp 1.000.000,—	,,	,,	Rp 1.500.000,—	45%
,,	Rp 1.500.000,—	,,	,,	Rp 2.000.000,—	47,5%
,,	Rp 2.000.000,—	,,	,,	Rp 2.500,000,—	50%
,,	Rp 2.500.000,—				52,5%

Before applying the rate, the taxable amount is to be round off downwards to the full amount of Rp 100,—

As from June 1964 this rate got a slight modification as shown below. This is necessary because of the severe rate of inflation at that time.

Taxable profit				Tax liability
		not over Rp	2.500.000,--	10%
over Rp	2.500.000	but not over Rp	5.000.000,—	20%
,, Rp	5.000.000	,, ,, ,, Rp	20.000.000,—	26%
,, Rp	20.000.000	,, ,, ,, Rp	40.000.000,—	32%
,, Rp	40.000.000	,, ,, ,, Rp	100.000.000,—	38%
,, Rp	100.000.000	,, ,, ,, Rp	250.000.000,—	44%
,, Rp	250.000.000	,, ,, ,, Rp	500.000.000,—	50%
,, Rp	500.000.000			52,5%

Due to the monetary reform, based on the Presidential Decree nr. 27, 1965, by which Rp 1.000,— old currency is revaluated at Rp 1,— the above mentioned rate underwent another amendment as follows:

Taxable profit				Tax liability
		not over	Rp 10.000,—	20%
over Rp	10.000,—	but not over	Rp 40.000,—	30%
,, Rp	40.000,—	,, ,, ,,	Rp 100.000,—	40%
,, Rp	100.000,—	,, ,, ,,	Rp 200.000,—	45%
,, Rp	200.000,—	,, ,, ,,	Rp 500.000,—	50%
,, Rp	500.000,—	,, ,, ,,	Rp 1.000.000,—	55%
,, Rp	1.000.000,—			60%

This rate is to be applied for the first time after June 30, 1966. to profits of the accounting year, ending

B. The tax rate laid down in article 11 of the C.T.A. was meant to be applied to profits received by newly established companies or corporate bodies. Within 5 years after establishment the following rate is applied:

Taxable profit				Tax liability
		not over	Rp 100.000,—	25%
over Rp	100.000,—	but not over	Rp 200.000,—	30%
,, Rp	200.000,—	,, ,, ,,	Rp 350.000,—	35%
,, Rp	350.000,—	,, ,, ,,	Rp 500.000,—	40%
,, Rp	500.000,—	the rate of article 10 is applied.		

Later on this rate is declared to be valid to the 5 years' exemption period. co-operative bodies, for profits enjoyed after

In June 1964 this rate has been altered totally. Henceforth the rate has been alleviated and is to be applied only to co-operative bodies after the 5 years' exemption period:

Taxable profit				Tax liability
	not over	Rp	1.000.000,—	5%
over Rp 1.000.000,—	but not over	Rp	5.000.000,—	10%
,, Rp 5.000.000,—	,, ,, ,,	Rp	10.000.000,—	15%
,, Rp 10.000.000,—				20%

C. In June 1966 article 10a has been added to the original article 10. Profits derived from the alienation of goods not intended for sale, if possessed by the company for more than 4 years and liquidation profit, either by dissolution or by merger, are subject to a flat rate of 10%.

TAX RETURN

The board of directors or the executive board of corporations, corporate bodies, juristic entities, cooperative bodies, organisations etc being subject to the Company tax, are required to file a return, even if they do not receive a return form from the Inland Revenue administration. A balance sheet and the income statement has to be attached to the return.

Tax returns must be filed within one month after the date of issue. If somebody is not able to file the tax return within the prescribed period, because he has not finished the drawing up of the balance sheet, he may file a provisional return with an estimated profit. In this case the final (definitive) return must be filed two months after finishing the balance sheet, but not later than the end of the year following the accounting year concerned.

Those who failed to file the return or neglected to file the tax return in accordance with the tax law, or made an incorrect return, by omitting any taxable income, are liable to punishment. For this purpose penalties are provided in both the administrative and judicial respects.

TAX ASSESSMENT

Normally the tax return is to be filed directly after expiration of the accounting year. The Company (corporation) tax can only be levied by assessment. The provisional assessment is levied according to the profit declared in the provisional return. The provisional assessment will be followed by the definitive asessment after the definitive return has been submitted to the tax authority.

By Act. nr. 22/1964 a new provision on assessment has been inserted being into force since June 30,1964. By this provision and since that date the possibility exists to levy a provisional assessment in the course of the accounting year, that is to say profits presumed to be made, could be taxed in advance. During the accounting year the provisional assessment can be levied only once by the tax authority, based on an estimated profit, but if the accounting year has expired and the provisional return has been submitted to the tax administration, indicating a higher profit, an additional provisional assessment could be levied in accordance with the profit declared.

If no tax is levied by the tax authority, intentionally or not, or the assessment is not in

accordance with the true facts, or by mistake a tax reduction/exemption has been granted, the tax authority can impose an additional assessment. An administrative sanction of 100% of the tax amount due would be added to the assessment if the cause of the default is on the side of the taxpayer.

THE SELF-ASSESSMENT SYSTEM

The self-assessment system is a new system being tried out. The executive board of companies, corporation etc is required to calculate itself the company tax due and pay the amount to the Tresury. For this purposes a special tax return form has been drafted and distributed to the taxpayers.

It could not be said beforehand whether the self-assessment system will be succesful. But anyhow the system gives a better prospect in the Company tax than in the income tax.

In case the self-assessment system is not obeyed by the taxpayer, the tax authority still reserves the right to levy a provisional assessment during the current accounting year.

TAX PAYMENTS/COLLECTION

Company tax, according to the definitive assessment must be paid within one month after the date of issue. (art. 36 par. 1)

As to temporary (provisional) assessments, distinction must be made between:

(a) the provisional assessment levied in the course of the accounting year;
(b) the provisional assessment levied after the expiration of the accounting year;

(a) The amount of tax of the provisional assessment levied in the course of the accounting year is payable in so many equal instalments, as the number of months of the accounting year is left, after the month in which the assessment notice has been issued. (art. 36 par. 3) Every payment is due on the 15th of each month. If the provisional assessment notice has been issued after the 7th month of the accounting year, the tax is payable in 5 equal instalments, starting from the month following the month of issue.

(b) If the provisional assessment il levied after expiration of the accounting year, the tax is payable in the same way as the definitive assessment (art. 36 par 1. see above)

When a taxpayer fails to pay tax in full by the date, an interest of 5% monthly must be paid on the unpaid amount from the due date till the date of payment.

Postponement of the payment of the tax could be granted to the taxpayer who can proof that the profit to be assessed will amount less than 3/4 of the amount which forms the basis of the provisional assessment.

The tax will be collected without delay in one operation,

(1) in case the company/corporation is in arrear for more than two instalments;
(2) in case of liquidation, winding up of the undertaking or in case of bankruptcy;
(3) in case the corporation ceases its activities, or is going to reduce the size of the undertaking, or it is going to alienate its real properties so that the due payment of the tax is endangered;
(4) in case a foreign body exercises an enterprise in Indonesia for the present;
(5) in case the properties owned by the company, organisations etc. have been attached by third parties.

TAX PENALTIES

Tax penalties are provided in the administrative sector as well in the judical sector.

Infringements or any defaults of the obligations described in the Tax Law such as a failure in filing the tax return or a failure in paying the tax on the due date, are punished by an administrative penalty will be a certain percentage of the tax amount due, and added

to the assessment so that it becomes an integrated part of the tax.
The judicial penalty is imposed by the judicial power upon tax crimes on conditions as law may prescribe. Some examples of tax crimes are given below:
(a) whoever knowingly or intentionally fils a false return will be punished with imprisonment not exceeding six months, if his action brings a loss upon the State;
(b) whoever knowingly or intentionally submits for investigation a false writing, pretending as if it is true and not false, will be punished with imprisonment not exceeding two years;
(c) whoever knowingly or intentionally infringes secrecy enjoined to him by article 44 C.T.A. will be punished with imprisonment not exceeding six months or with a fine not exceeding six hundred rupiah;
(d) whoever knowingly or intentionally fails to do his duty as set forth in article 43a, will be punished with imprisonment not exceeding three months or with a fine not exceeding five thousand rupiah.
If a taxpayer has not paid off the due tax, including the administrative sanction, the tax authority will attach the taxpayer's properties to be sold by auction or tender, or the taxpayer will be imprisoned for debt.

TAXATION OF FOREIGN COMPANIES

Foreign insurance companies having a permanent establishment in Indonesia are taxed according to the provision laid down in article 6 C.T.A. There are two alternatives:
(1) The profit of life insurance companies is fixed at 5% of the amount of premiums and capital received from the assured, having their domicile in Indonesia.
For other kinds of insurance companies, like fire insurance, transport insurance and accident insurance, the amount referred to is fixed at 10%.
(2) If requested by the taxpayer deviating from the provision set forth in article 6 (1) the profit of insurance companies, to be assessed is fixed on:

$$\frac{\text{(premium + capital) received from the assured in Indon.}}{\text{(premium + capital) received from the assured}} \times \text{total profit}$$

Foreign companies carrying on international transport business by ships or aircraft, and having income from such business derived from a permanent establishment in Indonesia are taxed on the basis of the formula:

$$\text{Income/profit} = 1/2 \times \frac{\text{(cargo + passenger from and to Indon.)}}{\text{total cargo + passenger}} \times \text{total profit}^{2})$$

TAX CREDIT/MEASURES TO PREVENT DOUBLE TAXATION

Article 8 C.T.A. provides a regulation which prevent double taxation. If in the taxable profit are included:
(a) profits from undertaking rendered by a permanent establishment abroad;
(b) profits derived from immovable properties situated abroad;
(c) interest from loans secured by a mortgage on immovables situated abroad;
then double taxation is avoided by deducting from the company tax, the tax on the income derived abroad, computed according to the provision of the Company Tax Act 1925.

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2) source: Asian Taxation 1964 p. 49. Japan Tax Association.

To prevent double taxation on national level, article 5 (2) paragraph 3 provides that certain types of interest on loans and payments for the right to use certain property, may not be deducted from the gross profit, when they are of an abnormal nature and result from a special relationship between the parties.

Article 5 (2) paragraph 5 provides that the sum paid to a company out of the profit is not deductible, save in the case of shares of the profits allocated to the State in some capacity other than that of a shareholder.

The amount which is not allowed to be deducted from the gross profit, of the payer, does not constitute the income of the recipient.

CLAIMS AND APPEAL

After preliminary inquiry by the district revenue offices all claims relating to the company tax have to be passed on to the head of the Inland Revenue Administration for decision (at present this is exercised by the Director of the direct taxes department).

Those who still have an objection against any decision, made by the executive branch (the director of the Direct Taxes Department) may appeal to the Board of Appeal for remedy within three months after the decision has been made.

What has been said relating disputes in Income tax, is applicable to Company tax accordingly.

FOREIGN INVESTMENT

To be complete I would like to mention in this context the tax allowances relating to the recently enacted Law on Foreign investment (Act nr. 1. 1967).

Foreign capital invested in Indonesia, with consent of the Indonesian government, in undertakings, not specially prohibited, enjoys a special tax relief.

(a) Company tax is not imposed on profits derived from invested foreign capital for a period not longer than five years, beginning the year of production;

(b) Profits derived re-invested foreign capital in undertakings in Indonesia are exempt from company tax for a period not longer than five years, beginning the year of re-investment;

(c) Tax at a flat rate of maximum 50% is imposed on profits for a period not longer than five years, after expiration of the exemption period;

(d) Losses suffered during the exemption period could be carried forward to profits received after the exemption period;

(e) To undertakings with foreign capital investment an accelerated depreciation is allowed;

(f) Profits received from undertakings with foreign capital investment could be transferred to the country of origin;

(g) Costs, salaries, renumerations of foreign employees employed in Indonesia could be transferred to the home country;

(h) Depreciation of machines, instruments, and equipment of undertakings with foreign capital investment could be transferred abroad.

DR. JUR. ROBERT HALPERN:

DIE ÖSTERREICHISCHEN WACHSTUMSGESETZE 1966

Unter dieser Sammelbezeichnung wurden im Juli 1966 7 neue Gesetze bezw. Gesetzesnovellierungen auf dem steuerlichen Sektor verabschiedet, welche im Bundesgesetzblatt vom 9. und 10. August 1966 verlautbart wurden. Es handelte sich dabei um folgende Bundesgesetze:

Körperschaftsteuergesetz 1966, Steuerliche Massnahmen bei der Kapitalerhöhung aus Gesellschaftsmittel, zwei Einkommensteuernovellen 1966, Umsatzsteuernovelle 1966, Nichterhebung der Wertpapiersteuer für inländische Schuldverschreibungen, neuerliche Abänderung des Versicherungssteuergesetzes 1953.

Während die zwei letztangeführten Gesetze nur einen sehr beschränkten Gesellschafts- bezw. Personenkreis betreffen und daher nicht von allgemeinem Interesse sind, sind die fünf erstgenannten Gesetze bezw. Novellen von allgemeiner Bedeutung. Über die angeführten steuerlichen Materien wurde zum Teil schon seit Jahren – unter der damaligen Sammelbezeichnung Kapitalmarktgesetze – innerhalb der österreichischen Koalitionsregierung verhandelt, ohne dass ein Einvernehmen erzielt werden konnte. Als auf Grund der Nationalratswahlen im März 1966 die österreichische Volkspartei im Nationalrat eine knappe, absolute Mehrheit erhielt, kam es nicht mehr zu einer Koalitionsregierung, sondern zu einer Einparteienregierung der österreichischen Volkspartei. Die neue Regierung beeilte sich nun, ihr steuerliches Konzept zu verwirklichen, so dass es schon im Juli 1966 zur Verabschiedung der angeführten Gesetze kam.

Die 1. und 2. Einkommensteuernovelle 1966 gingen in ihrem Inhalt wesentlich über die Novellierungen der fast regelmässig jährlich erfolgenden Einkommensteuernovellen hinaus. Sie brachten unter anderem zur Belebung der Investitionstätigkeit die Verankerung der vorzeitigen Abschreibung mit dem Regelsatz von 20% für unbewegliche Wirtschaftsgüter und 45% für bewegliche Wirtschaftsgüter im Einkommensteuergesetz – bisher wurden derartige Bestimmungen nur durch befristete Sondergesetze geregelt – die Berechtigung zur Bildung von steuerbegünstigten Investitionsrücklagen und eine allerdings reichlich komplizierte Neuordnung der Begünstigung des nicht entnommenen Gewinnes. Endlich wurden die Höchstbeträge für Sonderausgaben erhöht sowie Pauschbeträge für Sonderausgaben eingeführt und die Abzugsfähigkeit für Aufwendungen anlässlich der Neugründung eines Hausstandes wesentlich erweitert. Die Umsatzsteuernovelle brachte eine nunmehr unbefristete Neuregelung der Vorschriften über die sogenannte „Ausfuhrvergütung".

Die gegenständlichen neuen Bestimmungen sind teilweise ausserordentlich kompliziert und würden daher einer eigenen Abhandlung bedürfen, die zum Teil – international gesehen – nur einen kleinen Kreis von Spezialisten ansprechen würde. Im übrigen ist auf dem Gebiete der Einkommensteuer neuerlich eine Novellierung im Zuge.

So wollen wir uns im Folgenden nur mit jenen beiden Gesetzen näher befassen, welche die Körperschaften bezw. die Kapitalgesellschaften betreffen.

Die wesentlichen Neuerungen des Körperschaftsteuergesetzes 1966 betreffen eine neue Tarifregelung und die Einführung des sogenannten gespaltenen Körperschaftsteuertarifes; die im folgenden besprechenen neuen Bestimmungen treten erstmalig für die Veranlagung 1968 in Kraft.

Trotz der Bedeutung dieser neuen Bestimmungen führt der Motivenbericht zum Körperschaftsteuergesetz 1966 vor allem an, dass das vorliegende Gesetz „eine Zusammenfassung aller auf dem Gebiete des Körperschaftsteuerrechtes geltenden gesetzlichen Vorschriften darstellt. Durch diese Zusammenfassung soll erreicht werden, dass die Bestimmungen des geltenden Rechtes, die gegenwärtig in verschiedenen, nicht immer leicht auffindbaren Fundstellen verstreut sind, in einem Bundesgesetz zusammengefasst und dadurch für die Allgemeinheit leicht auffindbar werden. Damit wird der immer wieder vorgebrachten Beschwerde, dass der Rechtsstoff für die rechtsuchende Öffentlichkeit schwer zugänglich sei, nunmehr auch auf diesem Gebiete Rechnung getragen."

Wenden wir uns nunmehr den neuen Steuersätzen nach § 22, Abs.1 des Gesetzes zu: Bei den nun folgenden Angaben von Steuersätzen und Tarifvergleichen wurde der ab 1.1. 1967 in Kraft getretene 3%ige Zuschlag auf die Einkommen- und Körperschaftsteuer nach § 3 des Katastrophenfondsgesetzes bereits berücksichtigt. Die Ermässigung der Körperschaftsteuer wurde nunmehr so durchgeführt, dass bei gleichbleibenden Steuersätzen die Einkommensstufen verdoppelt wurden, also von bisher S 50.000.— auf S 100.000,—, von bisher S 100.000.— auf S 200.000.— und von bisher S 500.000.— auf S 1,000.000.—. Infolge dieser neu festgesetzten Einkommensstufen mussten auch die Grenzbeträge für die Anwendung der Härteklausel bei geringfügiger Überschreitung der festgesetzten Einkommenstufen geändert werden. Somit wird die Körperschaftsteuer einschliesslich des schon lange geltenden Beitrages von 18% und 3% bei einem Einkommen bis S 100.000.— 29.04%, bei einem Einkommen von S 113.700.— bis S 200.000.— 36.3%, bei einem Einkommen von S 250.100.— bis S 1,000.000.— 48.4% und endlich bei einem Einkommen über S 1,111.100.— 53.24% betragen. Die neuen Grenzbeträge von S 100.100.— bis S 113.600.— bezw. von S 200.100.— bis S 250.000.— werden entsprechend der bisherigen Regelung – wieder einschliesslich der Beiträge – mit dem Körperschaftsteuersatz von 29.04% bezw. 36.3% belastet zuzüglich 60.5% des S 100.000.— bezw. S 200.000.— übersteigenden Einkommens. Lediglich für die Zone von S 1,000.000.— bis S 1,111.100.— musste der Körperschaftsteuertarif auf 48.4% zuzüglich 48.4% des S 1,000.000.— übersteigenden Einkommens zurückgenommen werden; hätte man nämlich hier, wie es bisher bei den Einkommensstufen von S 500.000.— bis S 543.000.— der Fall gewesen ist, den 60.5%igen Satz belassen, so wäre dieses Mehreinkommen weiterhin – wie es bisher für das Mehreinkommen von S 500.000.— bis S 543.000.— tatsächlich der Fall war – mit 108.9% besteuert worden. Um die mit 1.1. 1968 in Kraft tretende Körperschaftsteuerermässigung besser beurteilen zu können, scheint ein kurzer Tarifvergleich zweckmässig.

Demgemäss wird sich die Körperschaftsteuer von dem seit 1950 geltenden Tarif, einschliesslich der 18%igen Beiträge zu dem ab 1.1. 1968 geltenden Tarif einschliesslich der Beiträge von 18% und 3% wie folgt ändern:

bei S	50.000.—	von S	14.160.—	auf S	14.520.—
bei S	100.000.—	„ S	35.400.—	„ S	29.040.—
bei S	200.000.—	„ S	94.400.—	„ S	72.600.—
bei S	500.000.—	„ S	236.000.—	„ S	242.000.—
bei S	1,000.000.—	„ S	519.200.—	„ S	484.000.—

Betrachtet man diese immerhin etwas überraschende Tarifentwicklung, so bleibt die Frage offen, ob nicht an Stelle der schematischen Verdoppelung der Einkommensstufen die Aufstellung eines neuen Schichtentarifes glücklicher gewesen wäre, wobei man auch die nicht befriedigende Besteuerung der Übergangseinkommenstufen hätte beseitigen können; sind diese doch von S 200.000.— bis S 250.000.— und von S 1,000.000.— bis S 1,111.000.— noch immer mit 96.8% besteuert, ein Prozentsatz, welcher kaum tragbar erscheint.

Wenden wir uns nunmehr dem § 22, Abs. 2 des Gesetzes zu, so bringt dieser Absatz die bedeutungsvollste Änderung im neuen Körperschaftsteuergesetz und zwar den sogenannten gespaltenen Körperschaftsteuersatz. Nach dieser Bestimmung ermässigt sich die Körperschaftsteuer auf die Hälfte des sich nach Absatz 1, also dem jetzt eingehend erörterten Normaltarif, ergebenden Betrages, soweit unbeschränkt steuerpflichtige Kapitalgesellschaften offene Ausschüttungen auf Grund eines den handelsrechtlichen Vorschriften entsprechenden Gewinnverteilungsbeschlusses vornehmen. Hierzu führt der Motivenbericht aus: „Der Ermässigung der Körperschaftsteuer für Ausschüttungen, die auf Grund eines den handelsrechtlichen Vorschriften entsprechenden Gewinnverteilungsbeschlusses vorgenommen werden, liegt die Erwägung zugrunde, dass die Rentabilität des in Kapitalgesellschaften angelegten Vermögens dzt. hinter der vergleichbarer anderer Kapitalanlagen, z.B. festverzinslicher Wertpapiere zurückbleibt und daher verbessert werden soll."

Somit beträgt der neue Körperschaftsteuersatz für ausgeschüttete Gewinne, wenn wir die Übergangsstufen aus Vereinfachungsgründen vernachlässigen, einschliesslich der Beiträge bis S 100.000.— 14.52%, bis S 200.000.— 18.15%, bis S 1,000.000.— 24.2% und darüber 26.62%.

Vergleicht man die wesentlich höhere Körperschaftsteuerermässigung für ausgeschüttete Gewinne in der Bundesrepublik Deutschland mit jener in Österreich, so bestehen dort 2 wichtige Sonderbestimmungen, welche in Österreich nicht eingeführt wurden. Das Körperschaftsteuergesetz der Bundesrepublik Deutschland kennt in seinem § 9 grundsätzlich das gleiche sogenannte Schachtelprivileg, welches in Österreich unverändert in § 10 des Körperschaftsteuergesetzes 1966 übernommen wurde. Tätigt nun eine unbeschränkte steuerpflichtige Kapitalgesellschaft in der Bundesrepublik Deutschland eine berücksichtigungsfähige Ausschüttung an eine Obergesellschaft, so wird auch diese Ausschüttung nur mit dem ermässigten Körperschaftsteuersatz von 15% belastet, obwohl diese Gewinnanteile bei Vorliegen der Voraussetzungen des Schachtelprivilegs bei der Obergesellschaft grundsätzlich körperschaftsteuerfrei wären. Schüttet nun die Obergesellschaft ihrerseits diese erhaltenen Gewinnanteile nicht aus, so werden sie mit einer besonderen Körperschaftsteuer, welche 36% beträgt, belastet. Die Begründung für diese sogenannte Nachsteur geht dahin, dass die Ausschüttung derartiger Gewinnanteile an eine Obergesellschaft nicht kapitalmarktfördernd wirkt, so dass die normale Besteuerung mit 51% gerechtfertigt erscheint.

Da das erwähnte Schachtelprivileg sowohl in der Bundesrepublik Deutschland als auch in Österreich entsprechend gilt, wenn Bund, Länder, Gemeinden, Gemeindeverbände oder Betriebe von inländischen Körperschaften des öffentlichen Rechts an unbeschränkt steuerpflichtigen Kapitalgesellschaften beteiligt sind, unterliegen offene Ausschüttungen einer unbeschränkt steuerpflichtigen Kapitalgesellschaft an diese Gebietskörperschaften in Österreich gleichfalls dem halben normalen Körperschaftsteuersatz

in der Bundesrepublik Deutschland dem Körperschaftsteuersatz von 15%. Diese Ausschüttungen bleiben bei den angeführten Gebietskörperschaften in Österreich unter den Vouraussetzungen des Schachtelprivilegs endgültig steuerfrei, während in der Bundesrepublik Deutschland von derartigen begünstigten Schachteldividenden einer Gebietskörperschaft eine besondere Kapitalertragsteuer von 25% im Abzugswege einbehalten wird, welche als Äquivalent für die fehlende Einkommensteuer des Anteilseigners bezeichnet wird. Diese beiden Formen der zusätzlichen Besteuerung für ausgeschüttete Gewinne, welche keinen kapitalmarktfördernden Charakter haben, gelten also nur in der Bundesrepublik Deutschland.

Als sonstige wesentliche Änderung wird die endlich erfolgte ersatzlose Aufhebung des § 17 des Körperschaftsteuergesetzes betreffend die sogenannte Mindestbesteuerung wohl allgemein begrüsst werden, da es sich hier um die Besteuerung eines fiktiven Einkommens handelte, welche in der Regel zu einer kaum tragbaren doppelten Körperschaftsteuerbelastung führte.

Die sonstigen sachlichen Änderungen im Körperschaftsteuergesetz 1966 sind nicht von allgemeinem Interesse und auch nicht sehr wesentlich, so dass auf eine Besprechung verzichtet werden kann.

Somit wenden wir uns dem Bundesgesetz vom 6.7. 1966 über steuerliche Massnahmen bei der Kapitalerhöhung aus Gesellschaftsmitteln zu. Der Motivenbericht zu diesem Gesetz führt im wesentlichen aus, dass bei einer steigenden Anzahl inländischer Kapitalgesellschaften das Nennkapital in einem Missverhältnis zu den Rücklagen und dem tatsächlichen Eigenkapital steht. Der Hauptgrund für diese Erscheinung wird einerseits in vorsichtigen Kapitalneufestsetzungen anlässlich der Schillingeröffnungsbilanz und andererseits in der sinkenden Kaufkraft der Währung gesehen. Die Folge des erwähnten Missverhältnisses ist ein auffallend starkes Ansteigen der Aktienkurse, fährt der Motivenbericht fort, wozu allerdings bemerkt werden darf, dass seit 1962 eine umgekehrte Bewegung der Aktienkurse festzustellen ist. Hohe Aktienkurse bewirken auch, dass breitere Schichten des kapitalanlagesuchenden Publikums vom Kapitalmarkt ferngehalten werden, wodurch die erstrebenswerte breite Streuung von Dividendenwerten und ihre marktkonsolidierende Funktion unterbunden wird. Das Missverhältnis zwischen Nennkapital und Rücklagen bezw. dem tatsächligen Eigenkapital kann durch eine Kapitalerhöhung aus Gesellschaftsmitteln beseitigt werden; einer derartigen Kapitalerhöhung standen aber bisher die Bestimmungen des Einkommensteuerrechtes im Wege. Gemäss § 20, Abs. 1, Z.1 Einkommensteuergesetz 1953 gehört der Bezug von Gratisaktien und Freianteilen zu den Einkünften aus Kapitalvermögen und unterliegen demnach der Einkommensteuer. Bekanntlich hat das Steuerrecht unterstellt, dass auch im Falle der Erhöhung des Eigenkapitals aus Gesellschaftsmitteln vorerst den Aktionären bezw. Anteilseignern Gratisaktien oder Freianteile zur Verfügung gestellt werden, welche dann zur Erhöhung des Kapitales verwendet werden. Somit sieht § 1 des Gesetzes folgendes vor: „Erhöht eine Aktiengesellschaft ihr Grundkapital (Nennkapital) oder eine Gesellschaft mit beschränkter Haftung ihr Stammkapital (Nennkapital) ausschliesslich aus Gesellschaftsmitteln, so unterliegt der Erwerb der neuen Anteilsrechte durch die Gesellschafter nicht den Steuern von Einkommen und Ertrag, wenn diese Kapitalerhöhung zwischen dem 1.1. 1967 und dem 31.12. 1970 beschlossen und durchgeführt wird." Dabei dürfen Rücklagen, die auf Grund besonderer Vorschriften steuerfrei gebildet wurden,

nicht für eine Kapitalerhöhung im Sinne der eben zitierten Bestimmungen verwendet werden. Ausdrücklich wird noch statuiert, dass derartige Kapitalerhöhungen keine Mindeststeuer im Sinne des Körperschaftsteuergesetzes auslösen, eine Bestimmung, welche für das Kalenderjahr 1967 noch erforderlich ist, da die früher erwähnte Aufhebung der Mindestbesteuerung entsprechend dem Inkrafttreten des Körperschaftsteuergesetzes erst ab 1.1. 1968 gilt.

Damit folgt dieses Gesetz ziemlich genau jener Resolution, welche anlässlich des letzten IFA-Kongresses in Lissabon zu diesem Thema gefasst wurde. § 2 des Gesetzes sieht vor, dass bei Erwerb neuer Anteilsrechte im Sinne des § 1 die 2%ige Gesellschaftsteuer vom Nennbetrag dieser neuen Anteilsrechte, also nicht im Sinne der Bestimmungen des Kapitalverkehrsteuergesetzes vom wohl regelmässig höheren Wert der neuen Anteilsrechte, zu berechnen ist.

§ 3 des Gesetzes befasst sich mit den Anschaffungskosten und sieht vor, dass die Anschaffungskosten der alten Anteilsrechte zusammenzurechnen und auf die alten und neuen Anteilsrechte im Verhältnis der Nennbeträge zu verteilen sind, wobei gegebenenfalls bei älteren Anteilsrechten die Bestimmungen des § 41, Abs.1 des Schillingeröffnungsbilanzengesetzes zu beachten sind. Aus dieser gesetzlichen Vorschrift folgt, dass sich durch den kostenlosen Erwerb dieser neuen Anteilsrechte keine Erhöhung der Anschaffungskosten ergibt.

Springen wir nunmehr zu § 5 des Gesetzes, so ist dort verankert, dass die Spekulationsfrist nach § 23 Einkommensteuergesetz 1953 hinsichtlich der zusätzlichen Anteilsrechte ab dem Erwerb der vor der Erhöhung des Nennkapitales erworbenen Anteils zu laufen beginnt; wenn im Gesetz auch nicht ausdrücklich verankert, so gilt diese Fristbestimmung wohl auch für eine Besteuerung gemäss § 17 Einkommensteuergesetz. Weiterhin sei darauf verwiesen, dass die Vorschriften des gegenständlichen Gesetzes sinngemäss auch für den Erwerb von Anteilsrechten an einer ausländischen Gesellschaft gelten wenn deren Rechtsform einer der im § 1 des Gesetzes bezeichneten Gesellschaftsformen entspricht. Jedesfalls wird aber, wie § 6 des Gesetzes ausdrücklich verlangt, der Erweber der neuen Anteilsrechte nachzuweisen haben, dass die Voraussetzungen für die steuerliche Behandlung nach diesem Bundesgesetz vorliegen, was bei ausländischen Kapitalgesellschaften vielleicht zu Schwierigkeiten führen kann.

Zum Schluss sei noch auf die Bestimmungen des § 4 des Gesetzes verwiesen, welcher im wesentlichen der Verhinderung von Missbräuchen dient. Setzt eine Kapitalgesellschaft innerhalb von 5 Jahren nach einer Kapitalerhöhung im Sinne des § 1 des Gesetzes das Nennkapital herab und zahlt sie die dadurch freiwerdenden Mittel ganz oder teilweise an die Gesellschafter zurück, so gelten diese Rückzahlungen insoweit als Gewinnanteile (Dividenden), als sie den Betrag der szt. Erhöhung des Nennkapitales nicht übersteigen. Ohne diese besondere gesetzliche Bestimmung würde die Rückzahlung vom Kapital anlässlich einer Kapitalherabsetzung kein steuerpflichtiges Einkommen, sondern einen gesellschaftsrechtlichen Vorgang darstellen, welcher verständlicherweise durch die eben erwähnte gesetzliche Vorschrift für einen Zeitraum von 5 Jahren nach Durchführung der Kapitalerhöhung einer einkommensteuerpflichtigen Ausschüttung gleich gehalten wird. Eine weitere Missbrauchsmöglichkeit würde bei dem entgeltlichen Erwerb eigener Anteilsrechte durch die Kapitalgesellschaft bestehen, weshalb Absatz 2 des § 4 festlegt, dass Beträge, die eine Kapitalgesellschaft innerhalb von 5 Jahren nach einer Kapitalerhöhung im Sinne des § 1 des Gesetzes für den

Erwerb eigener Anteile aufwendet, als steuerpflichtige Gewinnanteile (Dividenden) gelten, soweit die Nennbeträge dieser Anteile den Betrag der Erhöhung des Nennkapitales nicht übersteigen.

Die erwünschten und erforderlichen günstigen Auswirkungen dieser beiden Gesetze auf dem Kapitalmarkt lassen sich allerdings dzt. aus den abschliessend angeführten beiden Gründen noch nicht mit Sicherheit beurteilen. Das Körperschaftsteuergesetz 1966 gilt in seinen oben dargestellten neuen Bestimmungen, wie erwähnt, erstmalig für die Veranlagung 1968. Für das Bundesgesetz betreffend steuerliche Massnahmen bei der Kapitalerhöhung aus Gesellschaftsmittel fehlte ein handelsrechtliches Kapitalberichtigungsgesetz, welches erst soeben im Bundesgesetzblatt vom 13. Juni 1967 verlautbart wurde.

AGREEMENT BETWEEN THE GOVERNMENT OF INDIA AND THE GOVERNMENT OF GREECE FOR THE AVOIDANCE OF DOUBLE TAXATION OF INCOME

The Agreement for the avoidance of double taxation of income between Greece and India of February 11, 1965 has been ratified and Instruments of Ratification have been enchanged. The convention is effective in India for any year of assessment beginning on or after April 1, 1964 and in Greece for any year beginning on or after January 1, 1964. The text of the convention was published in The Gazette of India, March 25, 1967.

Whereas the Government of India and the Government of Greece desire to conclude an Agreement for the avoidance of double taxation of income:

Now, therefore, it is hereby agreed as follows:

Article i

(1) The taxes which are the subject of the present Agreement are:

(a) in India:
the Income-tax,
the Super-tax,
the Surcharge.
imposed under the Income-tax Act. 1961 (43 of 1961) (hereinafter referred to as "Indian Tax");

(b) In Greece:
the tax on physical persons and the incometax on legal entities, and any special tax levied in Greece with reference to freight earned by shipping enterprises by the carriage of passengers, live-stock or goods, imposed under the Royal Decrees No. 3323/1955 and 3843/1958 and the Law No. 1880/1951 (hereinafter referred to as "Greek Tax").

(2) The present Agreement shall also apply to any other taxes of a substantially similar character imposed in India or Greece subsequent to the date of signature of the present Agreement.

Article ii

(1) In the present Agreement, unless the context otherwise requires:

(a) the term "Greece" means the territory of the Kingdom of Greece;

(b) the term "one of the territories" and "the other territory" mean Greece or India as the context requires;

(c) the term "person" includes natural persons, companies and all other entities which are treated as taxable units under the tax laws in force in the respective territories;

(d) the term "company" means any entity which is treated as a body corporate or as a company for tax purposes;

(e) the term "tax" means the Greek tax or Indian tax, as the context requires;

(f) the terms "resident of Grecce" and "resident of India" mean, respectively, a person who is resident in Greece for the purposes of Greek tax and not resident in India for the purposes of Indian tax, and a person who is resident in India for the purposes of Indian tax and not-resi-

dent in Greece for the purposes of Greek tax. A company shall be regarded as resident in Greece if it is incorporated in Greece or its business is wholly managed and controlled in Greece; a company shall be regarded as resident in India if it is incorporated in India or its business is wholly managed and controlled in India.

(g) the terms "Greek enterprise" and "Indian enterprise" mean, respectively, an industrial or commercial enterprise or undertaking carried on by a resident of Greece and an industrial or commercial enterprise or undertaking carried on by a resident of India; and the terms "enterprise of one of the territories" and "enterprise of the other territory" mean a Greek enterprise or an Indian enterprise, as the context requires;

(h) the term "permanent establishment" means a fixed place of business in which the business of the enterprise is wholly or partly carried on;

(aa) the term "fixed place of business" shall include a place of management, a branch, an office, a factory, a workshop, a warehouse, a mine, quarry or other place of extraction of natural resources;

(bb) an enterprise of one of the territories shall be deemed to have a fixed place of business in other territory if it carries on in that other territory a construction, installation or assembly project or the like;

(cc) the use of mere storage facilities or the maintenance of a place of business exclusively for the purchase of goods or merchandise and not for any processing of such goods or merchandise in the territory of purchase, shall not constitute a permanent establishment;

(dd) a person acting in one of the territories for or on behalf of an enterprise of the other territory shall be deemed to be a permanent establishment of that enterprise in the first-mentioned territory, only if

1. he has and habitually exercises in the first-mentioned territory a general authority to negotiate and enter into contracts for or on behalf of the enterprise, unless the activities of the person are limited exclusively to the purchase of goods or merchandise for the enterprise, or

2. he habitually maintains in the first mentioned territory a stock of goods or merchandise belonging to the enterprise from which the person regularly delivers goods or merchandise for or on behalf of the enterprise or

3. he habitually secures orders in the first-mentioned territory wholly of almost wholly for the enterprise itself or for the enterprise and other enterprises which are controlled by it or have a controlling interest in it.

(ee) A broker of a genuinely independent status who merely acts as an intermediary between an enterprise of one of the territories and a prospective customer in the other territory shall not be deemed to be a permanent establishment of the enterprise in the last-mentioned territory.

(ff) The fact that a company, which is a resident of one of the territories, has a subsidiary company which either is a resident of the other territory or carries on a trade or business in that other territory (whether through a permanent establishment or otherwise) shall not, of itself constitute that subsidiary company a permanent establishment of its parent company.

(i) The term "pension" means a periodic payment made in consideration of services rendered or by way of compensation for injuries received;

(j) the term "annuity" means a stated sum payable periodically at stated times during life or during a specified or ascertainable period of time under an obligation to make the payments in return for adequate and full consideration in money or money's worth;

(k) the term "competent authority" means in the case of India, the Central Government in the Ministry of Finance, Department of Revenue, or its authorised representative and in the case of Greece, the Ministry of Finance or its authorised representative.

(2) In the application of the provisions of this Agreement in one of the territories any term not otherwise defined in this Agreement shall, unless the context otherwise requires, have the meaning which it has under the laws in force in that territory relating to the taxes which are the subject of this Agreement.

Article iii

(1) Subject to the provisions of paragraph (3) below, tax shall not be levied in one of the territories on the industrial or commercial profits of an enterprise of the other territory unless profits are derived in the first-mentioned territory through a permanent establishment of the said enterprise situated in the first-mentioned territory. If profits are so derived, tax may be levied in the first-mentioned territory on the profits attributable to the said permanent establishment.

(2) There shall be attributed to the permanent establishment of an enterprise of one of the territories situated in the other territory the industrial or commercial profits which it might be expected to derive in that other territory if it were an independent enterprise engaged in the same or similar activities under the same or similar conditions and dealing at arm's length with the enterprise of which it is a permanent establishment. In any case, where the correct amount of profits attributable to a permanent establishment is incapable of determination or the ascertainment thereof presents exceptional difficulties, the profits attributable to the establishment may be estimated on a reasonable basis.

(3) For the purposes of this Agreement the term "industrial or commercial profits" shall not include income in the form of rents, royalties, interest, dividends, management charges, remuneration for labour or personal services or income from the operation of ships or aircraft.

Article iv

Where—

(a) an enterprise of one of the territories participates directly or indirectly in the management, control or capital of an enterprise of the other territory, or

(b) the same persons participate directly or indirectly in the management, control or capital of an enterprise of one of the territories and an enterprise of the other territory, and

in either case conditions are made or imposed between the two enterprises, in their commercial or financial relations, which differ from those which would be made between independent enterprises, then any profits which but for those conditions would have accrued to one of the enterprises but by reason of those conditions have not so accrued may be included in the profits of that enterprise and taxed accordingly.

Article v

(1) Income derived from the operation of aircraft by an enterprise of one of the territories shall not be taxed in the other

territory, unless the aircraft is operated wholly or mainly between places within that other territory.

(2) Paragraph (1) shall likewise apply in respect of participations in pools of any kind by enterprises engaged in air transport.

Article vi

(1) When a resident of Greece, operating ships, derives profits from India through such operations carried on in India, such profits may be taxed in Greece as well as in India; but the tax so charged in India shall be reduced by an amount equal to 50% thereof, and the reduced amount of Indian tax payable on the profits shall be allowed as a credit against Greek tax charged in respect of such income. The credit aforesaid shall not exceed the Greek tax charged in respect of such income.

(2) (a) When a resident of India, operating ships, derives profits from Greece, through such operations carried on in Greece such profits may be taxed in Greece as well as in India; but the tax so charged in Greece shall be reduced by an amount equal to 50% thereof and the reduced amount of Greek tax payable shall be allowed as a credit against Indian tax charged in respect of such income. The credit aforesaid shall not exceed the Indian tax charged in respect of such income.

(b) Sub-clause (a) of clause 2 shall not, however, apply as long as the laws in Greece do not impose any tax on income derived from the operation of ships belonging to foreign enterprises operating in the Greek territory. In such cases, the profits referred to in sub-clause (a) of clause 2 may be taxed only in India.

(3) Paragraphs (1) and (2) shall not apply to profits arising as a result of coastal traffic.

(4) The provisions of clause (1) shall not in case of India affect the application of sub-sections (1) to (6) of section 172 of the Income-tax Act, 1961 for the assessment of profits from occasional shipping or tramp steamers; but the provisions of that clause will be applied, when an adjustment is to be made under sub-section (7) of the aforesaid section of the Income-tax Act, 1961 in such cases.

Article vii

Royalties derived by a resident of one of the territories from sources in the other territory may be taxed only in that other territory.

In this Article, the term "Royalty" means any royalty or other like amount received as consideration for the right to use copy-rights, artistic or scientific works, cinematographic films, patents, models, designs, plans, secret processes or formulae, trade-marks and other like property or rights, but does not include any royalty or other like amount in respect of the operation of mine, quarries or other natural resources.

Article viii

Dividends paid by a company which is a resident of one of the territories to a resident of the other territory may be taxed only in the first-mentioned territory.

Article ix

Interest on bonds, securities, notes, debentures or any other form of indebtedness, derived by a resident of one of the territories from sources in the other territory may be taxed only in that other territory.

Article x

Income from immovable property may be

taxed only in the territory in which the property is situated. For this purpose any rent or royalty or other income derived from the operation of a mine, quarry or any other place of extraction of natural resources shall be regarded as income from immovable property.

Article xi

Capital gains derived from the sale, exchange or transfer of a capital asset, whether movable or immovable, may be taxed only in the territory in which the capital asset is situated at the time of such sale, exchange or transfer.

Article xii

(1) Remuneration other than pensions and annuities, paid in Greece for services rendered therein out of public funds of India shall not be taxed in Greece unless the payment is made to a citizen of Greece.
(2) Remuneration other than pensions and annuities, paid in India for services rendered therein out of public funds of Greece shall not be taxed in India unless the payment is made to a citizen of India.
(3) The provisions of paragraphs (1) and (2) of this Article shall not apply to payments in respect of services in connection with any trade or business carried on by either of the Contracting Parties or political sub-divisions thereof for purposes of profit.
(4) The provisions of paragraphs (1) and (2) of this Article shall also apply to remuneration other than pensions and annuities paid by the Reserve Bank of India, the Public Railways Authorities and the Postal Administration of India and by the Bank of Greece, Greek State Railways and the Greek Postal and Telegraphic Administration.

Article xiii

Any pension or annuity derived by a resident of one of the territories from sources in the other territory may be taxed only in that other territory.

Article xiv

(1) Profits or remuneration for professional services or for services as an employee (including services as a director) performed in one of the territories by an individual who is a resident of the other territory may be taxed only in the territory in which such services are performed.
(2) An individual who is a resident of India shall not be taxed in Greece on profits or remuneration referred to in paragraph (1) if—
(a) he is temporarily present in Greece for a period or periods not exceeding in the aggregate 183 days during the calendar year immediately preceding the relevant fiscal year,
(b) the services are performed for or on behalf of a resident of India,
(c) the profits or remuneration are subject to Indian tax, and
(d) the profits or remuneration are not deducted in computing the profits of an enterprise chargeable to Greek tax.
(3) An individual who is a resident of Greece shall not be taxed in India on the benefits or remuneration referred to in paragraph (1) if—
(a) he is temporarily present in India for a period or periods not exceeding in the aggregate 183 days during the relevant "previous year",
(b) the services are rendered for or on behalf of a resident of Greece,
(c) the profits or remuneration are subject to Greek tax, and
(d) the profits or remuneration are not

deducted in computing the profits of an enterprise chargeable to Indian tax.

(4) Where an individual permanently or predominantly performs services on ships or aircraft in international traffic operated by an enterprise of one of the territories, profits or remuneration from such services may be taxed only by the country of which the individual is resident.

Article xv

A professor or teacher from one of the territories, who receives remuneration for teaching, during a period of temporary residence not exceeding two years, at a University, College, School or other educational institution in the other territory, shall not be taxed in that other territory in respect of that remuneration.

Article xvi

An individual from one of the territories who is temporarily present in the other territory solely—

(a) as a student at a university, college or school in such other territory,

(b) as a business apprentice, or

(c) as the recipient of a grant, allowance or award for the primary purpose of study or research from a religious, charitable, scientific or educational organisation shall not be taxed in the other territory in respect of remittances from abroad for the purposes of his maintenance, education or training in respect of a scholarship, and in respect of any amount representing remuneration for services rendered in that other territory, provided that such services are in connection with his studies or training or are necessary for the purpose of his maintenance.

Article xvii

(1) The laws in force in either of the territories will continue to govern the assessment and taxation of income in the respective territories except where express provision to the contrary is made in this Agreement.

(2) Subject to the provisions of Article VI income from sources within Greece which under the laws of Greece and in accordance with this Agreement is subject to tax in Greece either directly or by deduction shall not be subjct to Indian tax.

(3) Subject to the provisions of Article VI income from sources within India which under the laws of India and in accordance with this Agreement is subject to tax in India either directly or by deduction shall not be subject to Greek tax.

(4) The graduated rate of Greek tax to be imposed on residents of Greece and the graduated rate of Indian tax to be imposed on residents of India may be calculated as though income which under this Agreement is not subject to Greek or Indian tax, as the case may be, were included in the amount of the total income.

Article xviii

The competent authorities shall exchange such information (being information which is at their disposal under their respective taxation laws in the normal course of administration) as is necessary for carrying out the provisions of the present Agreement. Any information so exchanged shall be treated as secret and shall not be disclosed to any persons other than those concerned with the assessment and collection of the taxes which are the subject of the present Agreement. No information as aforesaid shall be exchanged by the competent authority of one of the territories which would disclose any trade,

business, industrial or professional secret or any trade process to the authority of the other territory.

Article xix

Where a resident of one of the territories shows proof that the action of the taxation authorities of the other territory has resulted or will result in double taxation contrary to the provisions of the present Agreement, he shall be entitled to present his case to the competent authority of the territory of which he is resident. Should his claim be deemed worthy of consideration, the competent authority to which the claim is made shall endeavour to come to an agreement with the competent authority of the other territory with a view to avoiding double taxation.

Article xx

(1) The present Agreement shall be ratified and the instruments of ratification shall be exchanged at New Delhi as soon as possible.
(2) Upon exchange of the instruments of ratification, the present Agreement shall have effect:--
(a) in India, for any year of assessment, beginning on or after the 1st April, 1964.
(b) in Greece, for any fiscal year, beginning on or after the 1st January, 1964.

Article xxi

This Agreement shall continue in effect indefinitely but either of the Contracting Parties may on or before the 30th day of June in any calendar year after 1965 give to the other Contracting Party notice of termination, and in such event this Agreement shall cease to be effective—
(a) in India, for any year of assessment beginning on or after the 1st April in the calendar year next following such written notice of termination,
(b) in Greece, for any fiscal year beginning on or after the 1st January next following such written notice of termination.

In witness whereof the undersigned duly authorised thereto have signed this Agreement and have affixed thereto their seals.

Done at New Delhi on the 11th February, 1965, in duplicate, in the English language.

For the Republic of India:
Sd/- RAMESHWAR SAHU,
Deputy Minister of Finance,
Government of India.

For the Royal Government of Greece:
Sd/- GEORGE WARSAMY,
Ambassador of Greece, New Delhi.

AGREEMENT FOR DOUBLE TAXATION RELIEF BETWEEN INDIA AND ADEN

THE INDIAN INCOME TAX (ADEN) RULES 1953

The Indian Income Tax Double Taxation Relief Aden Rules, 1953, dated March 24, 1953, continues to be in force by reason of section 297 (2) (k) of the Income Tax Act 1961.
They may be an example of the relief provisions mentionned in the article of Mr. P.L. Jaitly, *published on page 316 in this issue of the Bulletin.*

In exercise of the powers conferred by section 49A of the Indian Income-tax Act, 1922 (XI of 1922), and in supersession of the Notification of the Government of India in the late Finance Department (Central Revenues) No. 18-IT, dated the 21st February, 1942, the Central Government hereby makes the following rules for the grant of relief in respect of income on which tax has been paid both in the taxable territories and in Aden, namely:—

1. These rules may be cited as the Income-tax (Double Taxation Relief) (Aden) Rules, 1953.

2. In these rules,—

(a) the expression "Aden Income-tax" means Income-tax and Supertax charged for any year in accordance with the provisions of the Aden Income-tax Ordinance, 1951;

(b) the expression "Aden rate of tax" means the amount of Aden Income-tax divided by the amount of the income on which it was charged;

(c) the expression "Indian Income-tax" means income-tax and supertax chargeable, in accordance with the provisions of any law in force in the taxable territories;

(d) the expression "Indian rate of tax" means the rate determined by dividing the amount of income-tax paid in the taxable territories for the year in question by the amount of income on which tax was charged;

(e) the reference to the lower of the two rates shall, where the rates are equal, be construed as a reference to either of those two rates.

3. If any person, who has paid by deduction under section 18 of the Indian Income-tax Act, 1922, or otherwise, Indian income tax-for any year on any part of his income proves to the satisfaction of the Income-tax Officer that he has paid by deduction or otherwise Aden income-tax for that year in respect of the same part of his income, he shall be entitled to a refund calculated on that part of his income at a rate to be determined as follows:—

(i) if he is resident in the taxable territories the rate at which refund is to be given shall be:—

(a) The Aden rate of tax, when that rate does not exceed half of the Indian rate of tax, and

(b) half of the Indian rate of tax, in any other case;

(ii) if he is not resident in the taxable territories the rate at which refund is to be given shall be:—

(a) half of the Aden rate of tax when that rate does not exceed the Indian rate of tax, and

(b) in any other case the amount by

which the Indian rate of tax exceed half the Aden rate of tax.

4. (1) The application for refund of income-tax under these rules shall be made as follows:—

(i) If the applicant is resident in the taxable territories, to the Income-tax Officer of the District in which the applicant is chargeable directly to the Income-tax Officer of the District in which he ordinarily resides;*

(ii) If the applicant is resident outside the taxable territories, to the Income-tax Officer appointed by the Central Board of Revenue.

(2) Such application may be presented by the applicant in person or by a duly authorised agent or may be sent by post, and shall be in Form I* appended to these Rules.

5. No claim to any refund of Indian income-tax or super-tax under these rules shall be allowed unless it is made within four years from the last day of the financial year commencing next after the expiry of the previous year in which the income arose, accrued or was received or was deemed to have arisen, accrued or been received or was brought into the taxable territories.

6. An applicant for refund under these rules may appeal to the Appellate Assistant Commissioner of Income-tax from any order of the Income-tax Officer disallowing the claim for refund either wholly or in part.

7. The appeal shall be presented within thirty days of the date on which the order of the Income-tax Officer was communicated to the applicant, and shall be in Form II * appended to these rules.

*) Not printed here.

U.S. TAX CASE CREDITABILITY-U.K. TAX*)

The National Cash Register Company v. United States of America, U. S. District Court, Southern District Ohio, Western Division (April 7, 1967) is an extremely important decision relating to the creditability of the United Kingdom standard tax imposed in respect of dividends distributed to United States corporate stockholders.

THE FACTS

THE NATIONAL CASH REGISTER COMPANY ("NCR") during the year 1958, the (calendar) year here in question, owned all of the voting stock of two United Kingdom subsidiaries.

For the United Kingdom tax year beginning April 6, 1958, NCR's U.K. subsidiaries were subject to standard tax imposed at 38.75% and profits tax at 10%.

A U.K. corporation in 1958 could declare a dividend either "with deduction of standard tax" or "free of standard tax". A dividend "with deduction of standard tax" involved the distribution of the balance after the declared dividend had been reduced by the standard tax. In the case of a dividend "free of standard tax", the declared amount of the dividend was paid to the stockholder.

Pursuant to Article XIII of the Income Tax Convention between the U.S. and the U.K., as amended by the Supplementary Protocol of August 19, 1957 (effective for U.K. income tax years beginning April 6, 1956 through April 6, 1966), the standard tax "appropriate to" a dividend, being the amount by which a dividend from a U.K. corporation would have to be "grossed up", so that after deduction from the "grossed up" amount of the standard tax payable thereon, the amount received equalled the dividend received, was deemed to be the tax paid on the dividend, if the stockholder elected to include in his gross income the standard tax "appropriate to" the dividend. Consequently, a credit in respect of such tax paid was allowable under Section 901 of the Internal Revenue Code.

The dividends received by NCR from its U.K. subsidiaries in 1958 were declared "free of standard tax". The total dividends declared and received was approximately $2.6 million; the "grossed up" amount was approximately $4.23 million; and the standard tax "appropriate to" the dividend was approximately $1.6 million.

In its 1958 Federal income tax return, NCR claimed a direct credit in respect of the $1.6 million standard tax "appropriate to" the dividends received from its U.K. subsidiaries. It also claimed indirect credits under Section 902 in the amount of approximately $1 million computed according to the following formula:

$$\frac{\text{"Grossed-up Dividend"}}{\text{sub's "accumulated profits"}} \times \frac{\text{sub's "accumulated profits"}}{\text{sub's "total profits"}} \times \frac{\text{Taxes paid by the sub less standard tax}}{\text{"appropriate to" the dividend}}$$

*) Reported by Leo S. Ullman.

"Accumulated profits" consists of "total profits" less taxes paid by the U.K. subsidiaries. "Total profits" consists of pre-tax earnings. In the event that NCR would not be entitled to a credit as computed under the foregoing formula, it claimed in the alternative indirect credits under Section 902 according to the following formula;

$$\frac{\text{"Grossed-up Dividend}}{\text{sub's "accumulated profits"}} \times \frac{\text{sub's "accumulated profits"}}{\text{sub's "total profits"}} \times \frac{\text{Taxes paid by the sub less standard tax}}{\text{"appropriate to" the amount of its "accumulated profits"}}$$

Upon audit, the IRS reduced NCR's taxable income by the standard tax "appropriate to' the dividends, so that NCR's taxable income included only the amounts of the dividends declared and received, and it did not allow any direct credit in respect of U.K. taxes paid under the Convention. The IRS allowed a credit under Section 901 in the amount of approximately $1.3 million, being the total of indirect credits computed under Section 902, according to the following formula:

$$\frac{\text{Dividend received by NCR}}{\text{sub's "accumulated profits"}} \times \frac{\text{Sub's "accumulated profits"}}{\text{sub's "Total profits"}} \times \text{Total taxes paid by sub}$$

QUESTION PRESENTED

May a U.S. corporate stockholder which receives dividends from wholly owned U.K. subsidiaries and elects, under the Convention as then in effect, and Section 901, to claim a direct foreign tax credit for U.K. standard tax "appropriate to" those dividends also claim an indirect foreign tax credit under Section 902 for the remaining portion of the U.K. standard tax paid by the U.K. subsidiaries.

NCR'S ARGUMENT

NCR contended that under the Convention, it had the option of treating the standard tax "appropriate to" the dividends received as a withholding tax for which a 901 credit could be taken, provided the grossed-up amount was included in income, that in addition to the 901 credit it was entitled to an indirect credit for taxes "deemed paid", and that in computing the indirect credit it was entitled to take into account a proportionate part of the standard tax which was paid by U.K. subsidiaries but was not claimed, and could not be claimed as a credit under the Convention.

THE GOVERNMENT'S ARGUMENT

The Government contended that if a direct credit is claimed under the Convention for the standard tax "appropriate to" the dividend, then no part of the standard tax paid by the subsidiary can be included in the subsidiary's creditable taxes under Section 902. Conversely, the Government argued that if any standard tax paid by the U.K.

subsidiary was claimed as an indirect credit under Section 902, no direct credit under Section 901 could be claimed for that portion of the subsidiary's standard tax "appropriate to" the dividend.

HOLDING

The Court held that NCR could claim in addition to a direct foreign tax credit for the U.K. standard tax "appropriate to" dividends received from its U.K. subsidiaries, an indirect foreign tax credit under Section 902 for the remaining portion of the standard tax paid by the U.K. subsidiary. The Court did not indicate, however, which of the alternative formule used by NCR in claiming a 902 credit was applicable.

REASONS

The purpose of foreign tax credit provisions is to prevent double taxation of foreign source income.

The Convention made no reference to the remaining standard tax, i.e., the total standard tax paid by the U.K. subsidiary less the standard tax "appropriate to" the dividend, and therefore the remaining standard tax should be treated as a corporate income tax paid by the U.K. corporation, and treated in the same manner as the U.K. profits tax, the latter being admittedly properly creditable under Section 902. The Convention did not contemplate that a part of the standard tax should be excluded from favorable tax treatment as an indirect tax credit. Article XIII did not say or imply that only a part of the U.K. tax should be allowed as a credit.

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This third and extended edition providing a brief survey of Austrian income tax allowances with reference to the most recent case law on the subject.

Library International Bureau of
Fiscal Documentation, no. B 339.

CANADA

THE REPORT OF THE COMMISSION ON TAXATION;
Vol. I: Introduction, Acknowledgements, and Minority Reports- 1966;
Vol. II: The Use of the Tax System to Achieve Economic and Social Objectives – 1966;
Vol. III: Taxation of Income;
Vol. IV: Taxation of Income (continued);
Vol. V: Sales Tax and General Tax Administration;
Vol. VI: Implications of the Proposed Tax Reform.
Published by the Queen's Printer, Ottawa, 1966; 138, 353, 685, 848, 248 and 304 pp. resp.
The text of the Report of the Royal Commission on Taxation (Carter Report) prepared with a view to the revision of Canada's tax structure. The work is issued in 6 volumes. See TNS II-15 (1967) and Bulletin for International Fiscal Documentation, p. 201, no. 5 (1967).

Library International Bureau of
Fiscal Documentation, no. B 239.

E.E.C.

DER AUFBAU EINES EUROPÄISCHEN KAPITALMARKTS. Published by Europäische Wirtschaftsgemeinde, Brussels, November 1966, 421 pp.
The text of the so-called "Segre" Report which concerns the creation of a European capital market. Chapter 14 contains proposals in the field of the taxation of dividens and interest. See Bulletin for International Fiscal Documentation, p. 215, no. 5 (1967).

Library International Bureau of
Fiscal Documentation, no. B 334.

FRANCE

LE NOUVEAU REGIME DES RELATIONS FINANCIERES entre la France et l'étranger. Loi du 28 décembre 1966 et textes d'application. Published by l'Association nationale des sociétés par actions, Paris, 1967, 39 pp.
Commentary to the new French financial legislation regulating relations with foreign countries which entered into force as of January 31, 1967. The text of the Law, decrees and the regulations are appended.

Library International Bureau of
Fiscal Documentation, no. B 554.

GERMANY

BERLINER STEUERPRÄFERENZEN, by George, H. Published by Forkel Verlag, Stuttgart, 1966, 3rd revised and extended edition, 367 pp.
This edition of a book on tax incentives for individuals and enterprises located or doing business in West Berlin granted by way of reductions in the wage tax, individual and corporate income taxes, and the turnover tax and by way of other favourable provisions.

Library International Bureau of
Fiscal Documentation, no. B 321.

DIE FINANZREFORM UND DIE GEMEINDEN. Published in the series of the Verein für Kommunalwissenschaften e.V., nr. 14, Berlin, 1966, 147 pp., price DM 19,80.
This book is a collection of articles regarding the contemplated fiscal reform as it particularly affects the financial position of the municipalities. Authors such as Fritz Neumark, Wilhelm Heckt, Josef Kölbe, Adolf Hüttl, Herbert Timm, Bruno Weinberger, Willi Brundert and Karl Oettle, have contributed their views.

Library International Bureau of
Fiscal Documentation, no. B 319.

DIE UMSATZSTEUER, IHRE GESCHICHTE UND GEGENWÄRTIGE GESTALTUNG IM IN- UND AUSLAND, by Grabower, R. and D. Herting and G. Schwarz. Published by Carl Heymanns Verlag KG., Cologne, 1962, 2nd edition, 274 pp., price DM 34,50.
This second extended edition of the book—first published in 1925—providing a histoiical study of the evolution of the turnover tax system in different countries. Two additional chapters appear in this edition: the first concerns the new German TVA turnover tax system and a brief account of the turnover tax systems introduced in various countries since 1934.

Library International Bureau of
Fiscal Documentation, no. B 340.

GRUNDZÜGE DER STEUERLICHEN GEWINNERMITTLUNG, by Groener, L. and H. v. Wallis. Published by Carl Heymanns Verlag KG., Cologne, 1961, 3rd revised edition, 352 pp., price DM 32,—.
Work covering the principles for the computation of taxable profits. Examples are provided together with references to case law.

Library International Bureau of
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HANDBUCH ZUR EINKOMMENSTEUERVERANLAGUNG 1966. Published by Verlag des wissenschaftlichen Instituts der Steuerbevollmächtigten GmbH, Bonn and Verlag C.H. Beck, Munich and Berlin.
Guide to income tax assessment for 1966. The text of implementing regulations and directives are included together with commentaries thereto and examples.

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DIE VERANLAGUNG ZUR EINKOMMENSTEUER FÜR 1966. Einkommensteuergesetz und Einkommensteuer- Durchführungsverordnung mit Einkommensteuerrichtlinien, Rechtsprechung, Anweisungen, Anlagen. Published by Verlagsbuchhandlung des Instituts der Wirtschaftsprüfer GmbH, Düsseldorf, 1967, 633 pp.
These books form a sequal to the previous publications supplying guidance to the filing of 1966 corporate and individual income, business and turnover tax returns. The text of pertinent tax law provisions, rulings and regulations are also included. This volume pertains to the turnover tax, incorporating the amendments provided in the Amendment Law 1966 (Steueränderungsgesetz 1966), which became effective this year in view of its significance to economy. Volumes covering the following taxes are also available: Einkommensteuer für 1966; Körperschaftsteuer für 1966, Gewerbesteuer für 1966 and Umsatzsteuer für 1966.

Library International Bureau of
Fiscal Documentation, nrs. B. 491, B 490,
B 489 and B 497 resp.

DIE STEUERLICHE BEHANDLUNG EIGENER ANTEILE VON KAPITALGESELLSCHAFTEN, by Thiel, J. Published by Verlagsgesellschaft Recht und Wirtschaft mbH., Heidelberg in the series Steuerrecht und Steuerpolitik, nr. 6, 1967, 123 pp.
Redemption of stock by companies and GmbH and the taxation at the corporate and the shareholder level. Reference is also made to case law.

Library International Bureau of
Fiscal Documentation, no. B 558.

INTERNATIONAL

POLITIQUE ET MOYENS EMPLOYES PAR LES FINANCES PUBLIQUES en vue de la régularisation et de la croissance harmonieuse de l'économie (Public Finance Policy and Techniques for Economic Stability and Balanced Economic Growth). Published by Institut International de Finances Publiques, La Haye, 1966, 362 pp.
A collection of the various papers read at the "Budapest Congress", held by the International Institute of Public Finance.

Library International Bureau of
Fiscal Documentation, no. B 330.

ITALY

LAS TRANSFORMAZIONE DELL'IGE IN UNA IMPOSTA SUL VALORE AGGIUNTO, by Spalletta, E. Published by Edizioni Bizzarri, Rome, 1967, 150 pp.
Explanation of the consequences of changing the present multi-stage turnover tax system into a system of turnover taxation on value added; included is a survey of the French TVA.

Library International Bureau of
Fiscal Documentation, no. B 402.

TASSAZIONE DEGLI STRANIERI, by Piazza, G. Società e ditte estere. Investimenti di capitali esteri in Italia nelle imposte dirette. Published by Edizioni Consulente delle Aziende, 2nd edition, 382 pp.
Handbook to the taxation of foreign enterprises engaged in business activities or with investments in Italy. The texts of double taxation treaties and Ministerial decisions are also included.

Library International Bureau of
Fiscal Documentation, no. B 157.

NETHERLANDS

BELASTINGRECHT voor het examen moderne bedrijfsadministratie en het staatspraktijkdiploma, by Wempe, A.A. Published by J. Muusses N.V., Purmerend, 1967, 267 pp., 18th edition.
Text book of the Netherlands tax legislation for the Dutch administrative M.B.A. and S.P.D. examinations, including former examination papers.

Library International Bureau of
Fiscal Documentation, no. B 493.

HET FISCALE COMPROMIS, by Klein Wassink, H.J.W. Published by N.V. Uitgevers Mij. AE.E. Kluwer, Deventer-Antwerp, 1964, 218 pp.
A treatise on the juridical status of the compromis in tax matters, i.e. an agreement between the Revenue Department and the taxpayer, on certain points of dispute. The situation in the Netherlands is compared to that in Germany and the United States. A summary in English is appended.

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SWITZERLAND

DIE BESTEUERUNG VON AG UND GMBH IN DER SCHWEIZ (Betriebs-, Holding-, Beteiligungs-, Domizil- und Hilfsgesellschaften), Fachschriften der Handelskammer Deutschland-Schweiz, by Altorfer, W. Published by Trede & Co. Hamburg, 3rd revised edition, 1966, 175 pp.
This book updated the main work to January 1, 1966. It comprises a concise survey of Swiss taxation, including cantonal and municipal surcharges for ordinary, holding, domicilary and service companies.

Library International Bureau of
Fiscal Documentation, no. B 352.

KOMMENTAR ZUM ZÜRCHER STEUERGESETZ, by Reimann, A.F. Zuppinger and E. Schärrer. Gemeindesteuern, Strafbestimmungen und Schlussbestimmungen (§§ 135-203 StG) Published by Verlag Stämpfli & Cie., Bern, 1966, 564 pp., price S.Fr. 93,—.
Volume four of a commentary on the tax legislation in the Canton of Zurich, covering municipal taxes, penal provisions and final provisions relating to the tax treatment at the sale of immovable property. Material is updated to January 1, 1966. Volume three has still to be issued.

Library International Bureau of
Fiscal Documentation, no. B 329.

WEGWEISER DURCH DAS ST. GALLISCHE STEUERRECHT, by Weidmann, H. Published by Cosmos-Verlag A.G., Bern, 1967, 247 pp.
Commentary to the tax laws of the Canton of St. Gallen. The texts of the corporate and the individual income tax law and regulations thereto and of the succession duties law are also included.

Library International Bureau of
Fiscal Documentation, no. B 55.

UNITED KINGDOM

CLOSE COMPANIES, by Mus.oe, N.E. Published by Butterworths & Co., London, second edition, 1967, 346 pp.
This revised edition contains the amendments and additions made by the 1966 Finance Act and reflects the experience gained since the passing of the 1965 Financing Act with respect to the operation of the law relating to close companies. The number of examples has been increased and some topics (e.g. overspill relief and double taxation) are more widely discussed.

Library International Bureau of
Fiscal Documentation, no. B 492.

U.S.A.

FACTS AND FIGURES ON GOVERNMENT FINANCE. Published by the Tax Foundation, New York, 275 pp. 14th biennial edition, 1967, price $ 3.25.
Besides furnishing fiscal details with respect to operations of federal, state and local governments, this book supplies statistical and economic data on population, national output, income and prices and a newly expanded section on government social insurance programmes.

Library International Bureau of
Fiscal Documentation, no. 349.

AMERICAN FEDERAL TAX REPORTS. Second Series. Published by Prentice Hall, Inc., Englewood Cliffs, volume 18, 1967.
This volume contains the unabridged texts of federal and state court decisions concerning problems arising under the federal tax laws and previously reported in Prentice Hall federal taxes. This volume covers late cases decided under the 1954 Code with regard to income tax, estate and gift taxes and excise tax. Extensive cumulative tables including references to previous volumes and cross reference tables are appended.

Library International Bureau of
Fiscal Documentation, no. B 341.

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Joseph Otten, Liège.

CANADA

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FRANCE

CODE GENERAL DES IMPOTS, releases of July 15, 1966.
Ministère des Finances et des Affaires Economiques Imprimerie Nationale, Paris.
DICTIONNAIRE FISCAL PERMANENT, releases 10–12, 13, 13A, 14.
Editions Législatives et Administratives, Paris.
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GERMANY

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V.d. Linnepe Verlagsgesellschaft K.G., Hagen.
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INTERNATIONAL

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United Nations Organisation, Geneva.

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CODES MAROCAINS, RELEASES 1-3.
Fiduciaire Marocaine d'Editions Techniques, Casablanca.

NETHERLANDS

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L.J. Veen's Uitgeverij Mij. N.V., Amsterdam.
BELASTINGBERICHTEN, Supp. 80, 82A, 83, 84, 85, releases 86-90.
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LA LEGISLATION TURQUE, releases 3901-3925.
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UNITED KINGDOM

SIMON'S INCOME TAX SERVICE, Volume II A, release 54;
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Volume V, release 54.
Butterworth and Co. Ltd., London.

U.S.A.

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Commerce Clearing House Inc., Chicago.
FEDERAL TAXES REPORT BULLETIN, releases 11-20.
Prentice Hall, Inc., Englewood Cliffs, New Jersey.
FEDERAL TAXES REPORT BULLETIN - TREATIES, releases 11-12.
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XXIST IFA-CONGRESS HELD AT STOCKHOLM

The Stockholm Congress is over. The words of the Swedish Minister of Finance, Gunnar Sträng, in his opening address to the Congress were realised: Stockholm proved to be a pleasant Congress city and congressists were able to find time not only for work, but also for relaxation and sight-seeing; many old friendships were renewed and new friends made.
We shall remember the perfect organisation of the XXIst IFA-Congress and we wish to thank all persons responsible for its preparation and organisation.
Two draft resolutions were approved: The resolution on the first subject "Changes in the tax system as a part of stabilization policy—their technical and legal implications" was originally proposed in the English language; the resolution on the second subject "The development in different countries of the concept of a permanent establishment, notably from the point of view of harmonisation in future double taxation agreements" in French. The original text of the resolution on the first subject as approved, is published on page 424 of this issue of the Bulletin. The original text of the second resolution will be published in the October issue.

XXI CONGRÈS DE L'AFI TENU À STOCKHOLM

Le Congrès de Stockholm a eu lieu. Les mots du Ministre des Finances, Gunnar Sträng, dans son discours d'ouverture du Congrès se sont réalisés: Stockholm a prouvé qu'elle était une ville très agréable pour un Congrès et les Congressistes ont trouvé le temps de s'adonner au travail mais aussi de se détendre et d'admirer les beaux paysages. De vieilles amitiés se sont renouées et de nouvelles se sont créées.
Nous garderons le meilleur souvenir de la parfaite organisation du XXI Congrès de l'AFI et nous adressons nos plus vifs remerciements à ceux qui ont été les organisateurs. Les deux résolutions ont été approuvées. La résolution sur le premier sujet "Des modifications du système fiscal comme moyen de réaliser une politique de stabilisation, leurs implications sur le plan de la technique et de la légalité" proposée en langue anglaise; la résolution sur le deuxième sujet "Evolution dans les différents pays du concept d'établissement stable, notamment du point de vue de l'harmonisation dans les futurs accords sur la double imposition" en français.
Nous publions au page 424 la première dans le texte originel. La deuxième paraîtra dans le Bulletin d'octobre.

DR. J.C.L. HUISKAMP

* * * * ARTICLES * * * *

RONALD HOFFMAN*:

ESTIMATES OF EFFECTIVE TAX RATE DISTRIBUTIONS FOR HAWAII

I. INTRODUCTION

In 1959 Hawaii was admitted as the 50th of the United States. This group of (four main) Pacific islands, 2500 miles from the mainland coasts of California had been a U.S. territory since 1900. In many respects Hawaii appears as a developing appendage of the U.S., and therefore presents an interesting area for public finance research especially since "statehood, *per se* has had no effect on Hawaii's tax structure."[1]

This paper reports some estimates of the distribution of Hawaii state and local tax payments and effective tax rates.[2] Several sets of estimates have been prepared from the same basic data. This was done in order

a. to allow for competing hypotheses regarding tax shifting
b. to indicate the effect of allowance for tax deductibility and "export"
c. to include several income concepts.

These sets of estimates are presented below

1. for overall total taxes
2. for each of four major component taxes.

Data refers to the year 1960. Methods of estimation and effects of different assumptions are indicated to provide a basis for similar case investigations or comparative studies.

The results yielded by these different calculations emerge with a rather consistent pattern of characteristics. Briefly and roughly speaking, the middle income group of brackets ($5,000–$10,000, say) has the lowest rate assignments compared to brackets below and above this group. In addition, the brackets in this middle group are treated rather uniformly; that is, their rate assignments are fairly equal and so the overall tax rate structure is rather proportional in this income range.[3] The bottom income bracket (under

---

*) The author is Assistant Professor of Economics, University of Hawaii. This paper is based on the author's more detailed report to the Legislative Reference Bureau, University of Hawaii. Helpful suggestions are acknowledged from my colleagues Professors Robert Kamins, Harry Oshima, Edward Saraydar, John Wise, the participants in Ryuzo Sato's seminar on Quantitative Economics, and research assistant Gilbert Suzawa.

1 Y.S. Leong and R.M. Kamins, "Property Taxation in the 50th State, National Tax Journal, March, 1961, page 59.

2 Normative issues such as who ought to pay how much tax are not treated. A major deficiency is the absence of estimates of the distribution of benefits from public expenditure.

3 Note, however, that in order to delineate the five income brackets between $5,000 and $9,999, it was necessary to interpolate our income and expenditure data. For this reason, the interbracket detail of the result in this income range may not be as significant as that of the rest of the income scale.

$2,000) maintains a relatively high rate assignment. Some of the other characteristics of the distribution of rates are more sensitive to the different calculations, and these are given some attention below in the discussion of our results.

Section II presents some data on taxes and their distribution. Section III is concerned with alternative distributions of effective total tax rates based on adjusted gross income. Section IV considers rate distributions based on three other income concepts.

Section V discusses rate distributions for the major component taxes, and Section VI concludes the text. Appendix A discusses some bias.

II. TOTAL TAXES: TYPES, AMOUNTS, AND THEIR DISTRIBUTION

Table 1 shows the total tax collection information for the various taxes. Note that for each tax there are certain adjustments made to account for "tax exporting."[4] Also, note that there are separate columns for calculations based upon the conservative tax shifting assumption and the extensive shifting assumption. The meaning of and reason for these alternate assumptions will be discussed shortly. Table 2 shows percentage distributions of tax payments by tax types. The major component taxes are seen to be general excise (40%) personal income (18%), property (14%) and fuel tax (13%).[4-a]

Table 3 shows total overall taxes distributed among income size brackets. Four such distributions have been calculated, one for each shifting assumption, with and without the adjustment. The brackets are defined with respect to adjusted gross income.[5] The assignment of Hawaii state and local tax dollars to resident income by brackets was done tax by tax, and in fact most taxes were broken down into several sub-components which were then apportioned on an appropriate basis.[6] Briefly, taxes were assigned on

---

4 There are three aspects of the adjustment. One reflects the shifting of tax to non-residents via income use. All of our calculations include this one. The second allows for federal tax deductibility of certain state and local taxes. The third provides for tax shifting to non-residents via the source of income. Our calculations labelled "with the adjustment" include this latter pair. Space limitations for this paper do not permit the inclusion of details of the method and reasoning underlying the calculations, but these are available on request.

4a The general excise tax is a multistage affair. In 1960 the 3½% rate on gross revenues applied to almost all business activity with very few exceptions.

The personal income tax base is similar to the Federal counterpart. The 1960 rate schedule was: 3%, 3½%, 4%, 5%, 6%, 7% and 8%, on the first $500, next $500, next $1,000, next $3,000, next $5,000, next $10,000, and next $10,000, respectively, and 9% on over, $30,000.

The property tax is based on state assessed valuation, with rates set by the counties.

The fuel tax distinguishes among gasoline, diesel, and aviation fuel. The major portion is gasoline. Gasoline rates vary in the counties from 8½ to 11c per gallon.

5 Some implications of this definition are discussed in Appendix A.

6 Space limitations for this paper do not permit the inclusion of details of the method and reasoning underlying the calculations, but these are available on request.

TABLE I

TOTAL TAX

(Thousands of Dollars)

Name of Tax	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
	a) Total Collection	b)		Capital Outflow		e)		Total: (2)+(4)+(6)	Total: (3)+(5)+(7)	Net Assigned to Hawaii (1) - (8)	Net Assigned to Hawaii (2) - (9)
		c)	d)	c)	d)	c)	d)	c)	d)	c)	d)
General Excise	65837	5956	9791	10759	2115	7809	3147	24524	15053	41313	50784
Corporate Income	5068	0	0	2828	1885	1120	747	3948	2632	1120	2436
Bank	544	0	0	218	145	163	109	381	254	163	290
Personal Income	29871	0	0	0	0	3883	3883	3883	3883	25988	25988
Real Property	21871	417	1417	4035	889	3885	2204	8337	4510	13534	17361
Tobacco	2118	212	212	0	0	0	0	212	212	1906	1906
Fuel	20710	621	3921	4361	0	3781	1782	8763	5703	11947	15007
Public Utility	4242	199	398	738	0	598	0	1595	398	2647	3844
Liquor	3400	340	340	0	0	0	0	340	340	3060	3060
Insurance	1907	191	191	0	0	0	0	191	191	1716	1716
Estate & Inher.	1000	0	0	0	0	357	357	357	357	643	643
Unemployment Ins	4951	0	0	0	0	0	0	0	0	4951	4951
TOTAL f)	161519	7936	16270	22999	5034	21596	12229	52531	33533	108988	127986

a) Source: State of Hawaii, Director of Taxation, *Annual Report, 1960*
b) Sales to Fed. Government, Visitor Sales, and Export
c) Conservative Shifting Assumption
d) Extensive Shifting Assumption
e) Federal Tax Offset (Given that Outflow Occurs)
f) Columns may not sum to total due to rounding.

TABLE 2

COMPONENT TAXES

Proportion of Total Tax (Before and After Adjustment)

	(1)	(2)	(3)		(4)	
Name of Tax	Total Collection (Thousands of Dollars) a)	Percent of Total Collection	Net after Adjustment (Thousands of Dollars) b)	c)	Percent of Net b)	c)
General Excise	65,837	40.76	41.313	50,784	37.90	39.67
Corporate Income Tax	5,068	3.14	1,120	2,436	1.03	1.90
Bank Tax	544	.34	163	290	.15	.22
Personal Income Tax	29,871	18.49	25,988	25,988	23.84	20.30
Real Property Tax	21,871	13.54	13,534	17,361	12.42	13.56
Tobacco	2,118	1.31	1,906	1,906	1.75	1.48
Fuel	20,710	12.82	11,947	15,007	10.96	11.72
Public Utilities	4,242	2.63	2,647	3,844	2.43	3.00
Liquor	3,400	2.10	3,060	3,060	2.81	2.39
Insurance Tax	1,907	1.18	1,716	1,716	1.57	1.34
Estate & Inheritance Tax	1,000	.62	643	643	.60	.50
Unemployment Insurance	4,951	3.07	4,951	4,951	4.54	3.86
TOTAL	161,519	100.00	108,988	127,986	100.00	100.00

a) Source: State of Hawaii, Director of Taxation, Annual Report, 1960.
b) Conservative Shifting Assumption
c) Extensive Shifting Assumption

the basis of either the source or use of income. For example, the rental component of the general excise tax was assigned on the basis of income source (e.g., rental income and corporate income received in dividends) in the case of the conservative shifting assumption; under the extensive shifting assumption this assigment was based on income use (housing expenditure).

The objective of making calculations based upon (a) the conservative and (b) the extensive tax shifting assumptions was to construct a pair of extreme situations which would set limits for comparison. However, even under the (b) assumption of rather complete forward shifting, there are some component taxes for which zero shifting is assumed (e.g., the personal income tax). Similarly, under the (a) conservative assumption there are some components for which 100 percent forward shifting is assumed (e.g., the retailing portion of the excise tax). Thus, this pair of cases is not one of absolute extremes. Rather, each case is a combination of several "rather likely" assumptions (which we are somewhat more confident of) and several

TABLE 3

Total Tax: Dollar and Percentage Distribution of Total Tax By Income Brackets

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Income Bracket	Conservative Shifting Assumption Without Adjustment		Extensive Shifting Assumption Without Adjustment		Conservative Shifting Assumption With Adjustment		Extensive Shifting Assumption With Adjustment	
	$ Thousands	%	$ Thousands	%	$ Thousands	%	$ Thousands	%
Under $ 2000	6,751.3	4.41	9,003.6	6.21	5,722.9	5.26	8,784.9	6.86
$ 2000 - $ 2999	5,734.1	3.75	7,017.3	4.85	4,950.5	4.55	6,750.0	5.28
$ 3000 - $ 3999	9,739.8	6.37	11,340.4	7.83	8,290.2	7.63	10,870.2	8.50
$ 4000 - $ 4999	11,332.4	7.41	13,366.6	9.23	10,016.2	9.22	12,827.8	10.03
$ 5000 - $ 5999	9,630.9	6.30	12,099.9	8.36	8,868.0	8.16	11,733.1	9.17
$ 6000 - $ 6999	11,242.6	7.35	12,129.7	8.37	8,791.5	8.08	11,054.8	8.65
$ 7000 - $ 7999	9,881.2	6.46	10,378.3	7.17	7,474.6	6.88	9,341.3	7.30
$ 8000 - $ 8999	8,711.0	5.69	9,264.6	6.40	6,771.6	6.23	8,404.4	6.57
$ 9000 - $ 9999	7,079.6	4.63	7,544.2	5.21	5,554.1	5.11	6,917.7	5.41
$10000 - $14999	25,953.4	16.97	26,872.4	18.56	19,372.6	17.82	23,429.5	18.32
$15000 and over	46,873.6	30.66	25,790.1	17.81	22,879.9	21.06	17,785.8	13.91
TOTAL	152,930.0	100.00	144,807.0	100.00	108,692.0	100.00	127,900.0	100.00

extreme assumptions (about which we are somewhat more uncertain and therefore look at extreme opposites). In case (a) the extremes are all of the zero shift type, whereas in case (b) the extremes are 100 per cent forward shifting.[7]

7 An alternative procedure would have been to construct a case composed entirely of most likely assumptions about the shiftability of the excise components. This was not undertaken because it would have required rather extensive analysis to improve much on the information obtained from the "limit cases." The big obstacle to improvement here is the lack of empirical tests of tax shifting theories. This is especially true for a multistage tax such as the general excise. A considerable amount of knowledge about price determination in various markets would be necessary to systematically evaluate a shifting hypothesis. The complexity of the problem makes understandable the bareness of this shelf in the cupboard of economic literature.

III. EFFECTIVE TOTAL TAX RATE DISTRIBUTIONS BASED ON A.G.I.

Table 4 shows the distribution of average effective tax rates for overall total taxes. The term "average effective tax rate" is defined as the ratio: tax/income. There are four sets of estimates here as in Table 3. For each rate estimate entry in Table 4, the numerator is the corresponding tax entry in Table 3. The denominator (income) in each case is A.G.I. Table 5 shows the distribution of A.G.I. Some remarks regarding what has been "measured" appear in Appendix A. However, before turning to an examination of the results in Table 4, let us note here what we have in mind when we say that a tax is not shifted.[8]

A. SHIFTING

First of all, consider a sales tax, for example, and suppose it is levied and has impact on the seller of a product. The structure of relative prices of outputs and of inputs will generally undergo adjustment as a result of the imposition of a tax. This adjustment will result in an adjustment of real income flows and wealth stocks of the members of the community. For simplicity, suppose the adjustments proceed with fully employed resources from an initial position of equilibrium to a subsequent equilibrium. If we say the tax is not shifted what we have in mind is that the adjustment results in a decline, by the amount of the tax, in the real income (or perhaps the real present expected value of future income) of those who receive income as the seller of

8 See R.A. Musgrave, The Theory of Public Finance, McGraw Hill, 1959, Chapter 10.

TABLE 4

Total Tax: Average Effective Tax Rate By Income Bracket
(Based on Adjusted Gross Income)

Income Bracket	(1) Conservative Shifting Assumption without Adjustment		(2) Conservative Shifting Assumption with Adjustment		(3) Extensive Shifting Assumption without Adjustment		(4) Extensive Shifting Assumption with Adjustment	
	Percent	Rank	Percent	Rank	Percent	Rank	Percent	Rank
Under $ 2000	17.11	2	14.50	1	22.81	1	22.26	1
$ 2000 - $ 2999	11.89	5	10.26	5	14.55	5	13.99	3
$ 3000 - $ 3999	11.60	6	9.88	6	13.51	6	12.95	5
$ 4000 - $ 4999	12.53	4	11.08	3	14.78	4	14.18	2
$ 5000 - $ 5999	10.04	11	9.24	7	12.61	7	12.23	6
$ 6000 - $ 6999	10.99	8	8.59	10	11.86	9	10.81	8
$ 7000 - $ 7999	11.38	7	8.60	9	11.95	8	10.75	9
$ 8000 - $ 8999	10.44	10	8.12	11	11.10	11	10.07	11
$ 9000 - $ 9999	10.99	9	8.62	8	11.72	10	10.74	10
$10000 - $14999	14.42	3	10.76	4	14.93	3	13.02	4
$15,000 and over	29.29	1	14.30	2	16.12	2	11.11	7
Overal total	14.78	(3)	10.50	(4-5)	13.99	(5-6)	12.36	(6)

TABLE 5

Dollar and Percent Income Distribution Based on Different Income Concepts

Income Bracket	(1) Adjusted Gross Income		(2) Adjusted Gross Income Minus Federal Taxes		(3)		(4) Broadened Income		(5)		(6) Broadened Income Minus Federal Taxes		(7)	
	$ Thou-sand	%	a) $ Thou-sand	%	b) $ Thou-$sand	%	a) $ Thou-sand	%	b) $ Thou-sand	%	a) $ Thou— %	%	b) $ Thou-sand	%
Under $2000	39,464	3.78	32,376	3.80	30,076	3.68	55,014	4.40	54,238	4.40	44,700	4.65	42,351	4.50
$ 2000 - $ 2999	48,238	4.70	40,031	4.75	38,550	4.60	70,981	5.65	70,476	5.70	60,064	6.20	58,551	6.20
$ 3000 - $ 3999	83,946	8.10	70,238	8.35	68,017	8.35	104,018	8.30	102,982	8.40	85,066	8.80	82,779	8.90
$ 4000 - $ 4999	90,436	8.70	75,338	8.95	72,932	9.00	105,476	8.35	104,634	8.50	85,484	8,80	83,024	8.90
$ 5000 - $ 5999	95,949	9.25	81,055	9.65	78,587	9.70	105,565	8.45	105,266	8.50	87,503	9.15	85,017	9.10
$ 6000 - $ 6999	102,300	9.85	85,960	10.20	83,414	10.20	115,264	9.15	113,760	9.20	92,545	9.55	89,904	9.65
$ 7000 - $ 7999	86,864	8.40	72,753	8.70	70,602	8.75	98,015	7.80	96,487	7.80	78,153	8.10	75,904	8.15
$ 8000 - $ 8999	83,434	8.30	70,075	8.35	68,248	8.35	90,924	7.15	89,749	7.30	72,937	7.60	71,036	7.60
$ 9000 - $ 9999	64,394	6.20	54,022	6.40	52,505	6.35	70,526	5.60	69,565	5.70	56,550	5.80	54,971	5.90
$10000 - $14999	179,990	17.40	145,179	17.30	139,585	17.20	199,124	15.80	195,590	15.90	152,498	15.70	146,679	15.70
$15,000 & over	160,025	15.40	115,179	13.70	111,748	13.80	243,334	19.50	225,648	18.50	148,812	15.50	144,253	15.60
TOTAL	1,035,039	100.08	842,206	100.15	814,264	99.98	1,258,241	100.15	1,228,398	99.80	964,312	99.85	934,469	100.20

NOTE: Columns may not add to totals due to rounding
a) Conservative Shifting Assumption
b) Extensive Shifting Assumption

the product. On the other hand, if we say that the tax has been completely shifted forward to the consumer, what we mean is that the adjustment results in a decline, by the amount of the tax in the real income of those who use their income to purchase the product whose sale is subject to the tax levy. A somewhat broader view would consider the adjustment which results not only from the imposition of the tax but also the expenditure of the tax revenue by the government.

Now, in terms of our study, the calculations of the ratio of tax/income suggests the following. The observed income occurs as the result of adjustment to both the imposition of the tax and the expenditure of the tax revenues. The calculated tax assignments to both sources and uses of income represent reductions in income available for expenditure on goods and services other than those rovi ded by the taxing authority. That is, the calculated tax assignments (to the income brackets) represent shares of the cost of expenditures made by Hawaii state and local governments. It should be noted that the same A.G.I. income distribution was used in the tax rate calculations under both the conservative and the extensive shifting assumptions. This implies the assumption that the income distribution is independent of the shiftability of taxes.[9]

Let us examine the results in Table 4. From an equity point of view, with income as the relevant index of equality, the ability to pay consideration is manifested in the relation of tax to income. Our interest is centered on the ratio of tax to income (that is, the average effective tax rate), because our position is that it is the relation of tax payment to income, whatever its source, which is relevant, rather than a so-called balance among taxes on personal income, business income, property, etc. The feature of our rate estimates which deserves emphasis is the pattern of relative positions; it is the picture of how these rate estimates stack up one against another—which income bracket has the highest rate, which bracket next and by how much—that seems to be of primary importance.

B. REFERENCE CASE

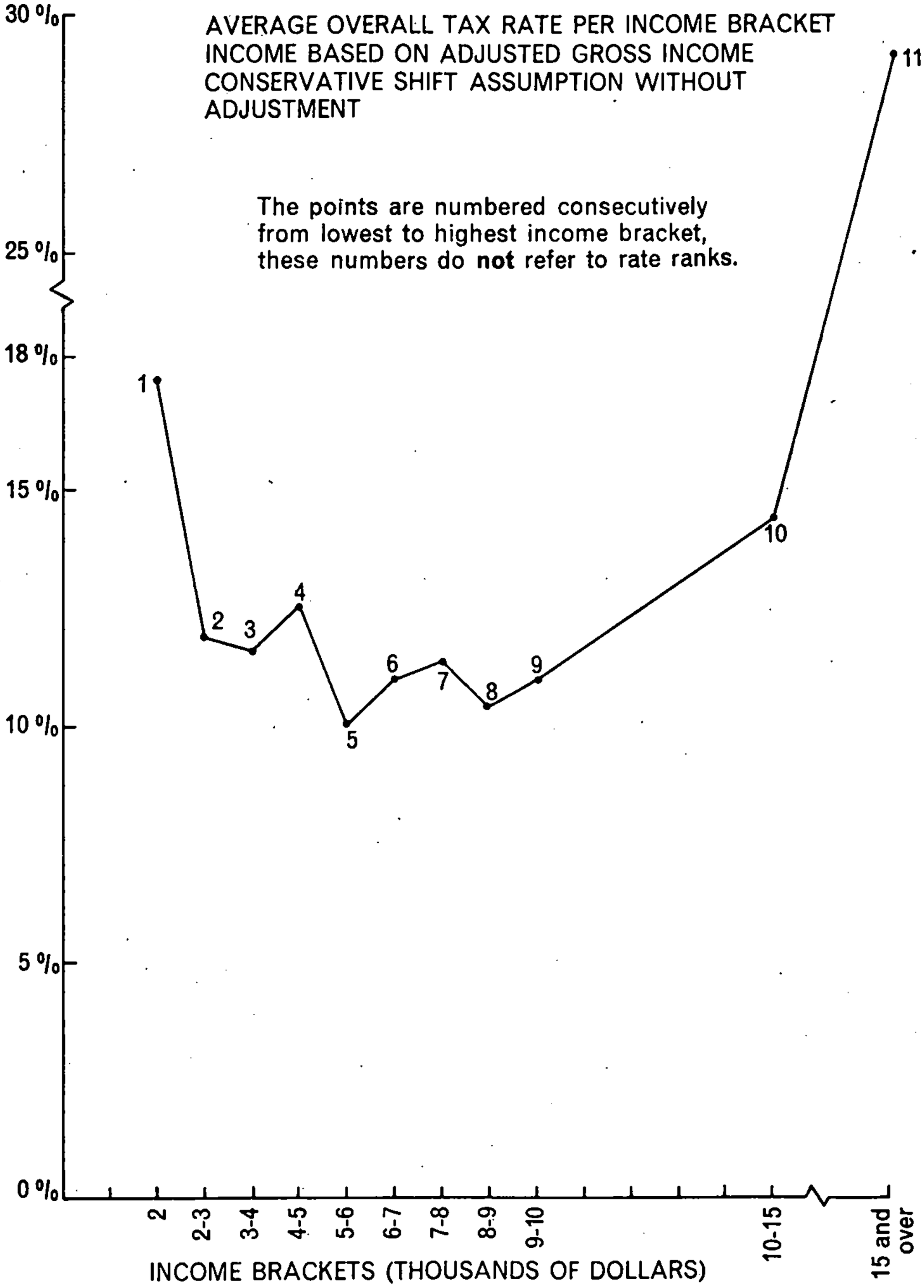
Consider column 1 in Table 4. The % entries are the average effective rate estimates. The rank entries are based on the rates, with rank #1 assigned to the income bracket with the highest rate, and rank #11 assigned to the bracket with the lowest rate. These rate calculations involve the conservative shifting assumption without the adjustment for tax deductibility and ownership, and will be designated as the reference case.[10] Graph 1 is a picture of the information in column 1 of Table 4. The eleven points in the graph space are consecutively numbered from 1 (for the under $2,000 bracket) to 11 ($15,000 and over); these numbers do not refer to ranks. The vertical position of each point indicates the tax rate calculated for the income bracket, and the points are connected by line segments to facilitate reading.

We note the rather high rate position (at 17%) of bracket number 1 (the under $2,000 bracket), the cluster of brackets 2, 3, and 4 in lower position (at 12%), the cluster of

9 We settled for this assumption. The A.G.I. distribution may be modified by the addition of appropriate amounts of unshifted taxes to each income bracket. We did this but the results did not show any significant change.

10 No normative significance is implied. We merely designate a point of reference to facilitate making comparative statements. The reference case is to be viewed as the "least adjusted case" and not necessarily as the "preferred or more reasonable case."

GRAPH 1


AVERAGE OVERALL TAX RATE PER INCOME BRACKET
INCOME BASED ON ADJUSTED GROSS INCOME
CONSERVATIVE SHIFT ASSUMPTION WITHOUT ADJUSTMENT
The points are numbered consecutively from lowest to highest income bracket, these numbers do **not** refer to rate ranks.
AVERAGE OVERALL TAX RATES (PERCENTAGE)
30 %
25 %
18 %
15 %
10 %
5 %
0 %
1
2
3
4
5
6
7
8
9
10
11
2
2-3
3-4
4-5
5-6
6-7
7-8
8-9
9-10
10-15
15 and over
INCOME BRACKETS (THOUSANDS OF DOLLARS)

brackets 5 through 9 in lowest position (at 11%), and the higher position of brackets 10 (at 14%) and 11 (at 29%). Given the degree of precision in these estimates one is inclined to "smooth out" the rate difference among the brackets 2, 3, and 4, and among the brackets 5 through 9. This smoothing reveals a horseshoe or "U" shaped curve with bracket number 1 on the upper left hand corner, bracket number 11 on the upper right hand corner, and the rather flat bottom of the curve running between $5,000 and $9,999.[11] In terms of the ranks in column 1 of Table 4, the last five ranks (7 through 11) are occupied by the five brackets between $5,000 and $9,000, i.e., bracket numbers 5 through 9. The top income bracket (number 11) has the highest rate and therefore so has rank 1, and the bottom bracket (number 1) has rank 2. Thus this pattern of estimates indicates that the overall tax rates are relatively high for the income brackets at the extremes of the income scale, and relatively low and invariant for the brackets in the middle of the income scale. In rough terms, the rate structure is regressive, proportional, and progressive at the low end, the middle, and the high end of the income scale respectively.

Before turning to other estimates for overall tax rates, let us summarize some of the details of the rate structure for the reference case.

1. The rates range from about 10% to 29%, with a 3 to 1 ratio between ranks 1 and 11.
2. The rate spread between ranks 1 and 2 is about 12 percentage points, but between ranks 2 and 3 it is only about 2½ points, and from ranks 3 to 11 inclusive the rate spread is about 4 percentage points. The smaller the spread, the closer is the rate structure to proportionality.
3. For all income brackets taken together, the rate is 14.8%, quite close to the rate for the $10,000–$14,999 bracket.
4. The four brackets at the low end of the income scale represent about 25% of the income (A.G.I.) and bear an assignment of about 22% of the tax. The bottom bracket alone shows 3.8% of the income and 4.4% of the tax. The ranks run from 2 to 6, with the three brackets between $2,000 and $4,999 receiving fairly proportional treatment. The pair of top income brackets accounts for about 33% of the income and has about 48% of the tax assigned to it in the reference case. The middle income group percentages run 42% and 30% for income and tax respectively.[12]

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11 Due to data insufficiency, there is not much that can be said about how far the range of "relative proportionality" of the $5,000 to $9,999 group extends into $10,000 to $14,999 bracket. However, we have a relationship between cumulative tax and cumulative income. This relationship is actually derived from the pair of relationships between (a) cumulative tax and income, and (b) cumulative income and income. There are data for eleven points on each of these relationships, and by connecting these points with a smooth freehand curve it is possible to estimate the extension of the range of "relative proportionality." An estimate on this basis is that the range runs to about the $12,500 income level, and thus covers cumulative income from $262 million ($5,000 to $5,999 bracket) to about $820 million, a range of over $550 million which accounts for over half the income in total. See footnote 2 above regarding the effect of interpolation.

12 The ratios of percent of tax/percent of income for these income bracket groups are another way to summarize the rate structure.

Income Bracket Group	Percent of tax/percent of income
4 lowest income brackets	88%
bottom bracket alone	
5 middle income brackets	71%
pair of top brackets	145%

Now let us turn to the alternate calculations of the overall total tax rate distributions based on A.G.I., which appear in columns 2, 3, and 4 of Table 4. We are interested in comparisons with the reference case, and Graph 2 is helpful in this regard. Here the line of thick solid segments repeats the reference case from Graph 1. The tree other lines represent the other cases.

C. CONSERVATIVE WITH ADJUSTMENT

The line (– – –) refers to the conservative shifting assumption, with the adjustment (see column 2, Table 4). As compared to the reference case, the "U„ shape remains, but the whole curve has shifted down and lies at a lower rate level, and this shift is not uniform through the income range. This change is due to the nature of the adjustment, which has two main aspects. One—deductibility—is recognition of the fact that certain state and local taxes are deductible for federal personal and corporate income tax purposes. The other—ownership—is the allowance for non-resident ownership of business enterprises which bear Hawaii state and local taxes.

The total amount of tax to be dealt with here is about ⅓ lower than in the reference case and so all rates are lower, the ratio of highest to lowest rate has dropped to less than 2 to 1, and rate differences in the group of middle income brackets are smaller. In general, the adjustment has a more pronounced effect on the higher income brackets because of the progressivity of the federal income taxes and the positive relation between income size and the proportion of non wage income. Rank shifting, which is minimal, includes the movement of the bottom-most income bracket into rank, 1, with the top rate of 14.5%.

D. EXTENSIVE WITHOUT ADJUSTMENT

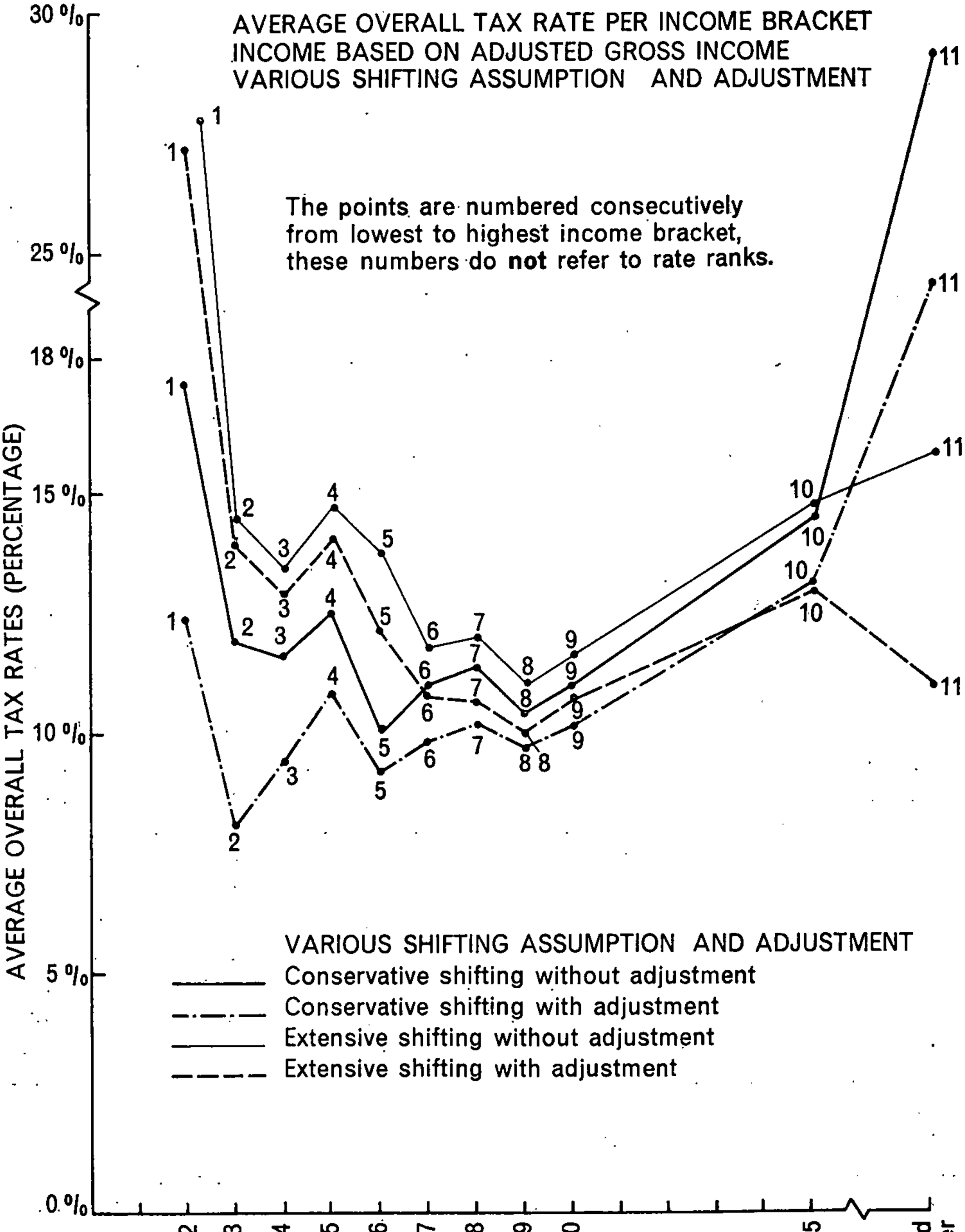
Turning now to the rates based on the extensive shifting assumption, without the adjustment, consider column 3, Table 4, and the line of thin solid segments in Graph 2. Again, as compared to the reference case, the "U" shape remains. However, the upper left-hand corner (bracket number 1) is markedly higher at a 23% rate, and the upper right-hand corner bracket number 11) is much lower (50 per cent) at a 16% rate. The "U" has shifted up, non uniformly, to higher rates for all except the top income bracket. Generally, the difference in results is as expected. When the conservative shifting assumption is replaced by an assumption of more extensive forward shifting of taxes,[13] larger amounts of tax enter our calculations on the basis of use of income, and smaller amounts are assigned on the basis of source of income.[14] Data regarding expenditure patterns (income use) indicates that lower income brackets spend larger proportions of their income on taxable items than do higher income brackets.[15] Data regarding the source distribution of income indicates that higher income brackets receive larger proportions of income from non wage sources (such as profits, rentals, etc.) than do lower income brackets. Thus the change in shifting assumption results in larger amounts of tax being "removed" from the higher relative to the lower income brackets (on the income source side) and smaller amounts of tax being "placed upon" the higher relative to the lower income

13 I.e., shifting from the impactee upon whom the tax is levied, to the other party in the transaction involving the item which is taxed.

14 Because the tax is shifted from "seller" to "buyer", or from "business" to "consumer".

15 See footnote 24 below. Also see Appendix A regarding the expenditure and the income data.

GRAPH 2


AVERAGE OVERALL TAX RATES (PERCENTAGE)
30 %
25 %
18 %
15 %
10 %
5 %
0 %
AVERAGE OVERALL TAX RATE PER INCOME BRACKET
INCOME BASED ON ADJUSTED GROSS INCOME
VARIOUS SHIFTING ASSUMPTION AND ADJUSTMENT
The points are numbered consecutively from lowest to highest income bracket, these numbers do not refer to rate ranks.
VARIOUS SHIFTING ASSUMPTION AND ADJUSTMENT
Conservative shifting without adjustment
Conservative shifting with adjustment
Extensive shifting without adjustment
Extensive shifting with adjustment
2
2-3
3-4
4-5
5-6
6-7
7-8
8-9
9-10
10-15
15 and over
INCOME BRACKETS (THOUSANDS OF DOLLARS)

brackets (on the income use side). Therefore the change in shifting assumption results in relatively higher tax rate estimates for the lower income brackets as compared to the higher brackets.

A major feature of the rate estimates in column 3 is the outstanding position of the lowest income bracket. It has the highest rate, and this rate is substantially higher than either the next highest rate (that of the uppermost income bracket), or the rate of the adjacent income bracket ($2,000–$2,999).

The ratio of highest to lowest rate in this set of calculations is about 2 to 1. The major portion of this "narrowing" (as compared with the reference case) occurs mainly between ranks 1 and 2. In the reference case (column 1) the top income bracket has rank 1, and the bottommost bracket has rank 2. These rank assignments are reversed in both column 2 and column 3 of Table 4. However in column 2 this reversal occurs with a decrease in the lowest income bracket rate, but in column 3 the bottommost bracket rate is substantially increased (with respect to the reference case). Thus we note an important dissimilarity between the effect of introducing the adjustment, as compared to changing to the extensive shifting assumption.

Note also that the top two income brackets occupy ranks 2 and 3, with a spread of only about 1 percentage point between their rates. This is in marked contrast to the 14 percentage point spread and the 2 to 1 ratio of rates found in column 1. The more extensive tax shifting assumption has closed this gap, to an even greater degree than did the adjustment for tax deductibility and ownership.

Clearly, the pair of changes in the basis for calculation (the shifting assumption on the one hand, and the adjustment on the other) are not of the same general nature. Use of the extensive shifting assumption results in the top income bracket experiencing a rate decline at the non-uniform expense of all other brackets—each of which has a tax assignment that is larger than in the reference case, but not by the same amount (or proportion). The rather regressive nature of the effect of the extensive shifting assumption shows up in the comparison of the rates for a given income bracket under the two shifting assumptions.

E. EXTENSIVE WITH ADJUSTMENT

The results obtained with employment of both the extensive shifting assumption and the adjustment are shown in column 4 of Table 4, and by the line of dashed ( ) segments in Graph 2. The shape of the rate pattern again resembles a "U", but there are noticeable differences from the reference case. The left-hand extreme rate is higher, and the positions of bracket numbers 10 and 11 have fallen (and reversed). The rates assigned to all the income brackets up through $5,999 are higher than in the reference case, while the rates for all income brackets above $6,000 are lower.

The lowest income bracket has rank 1 with a 22% rate. Further, that rate is twice as high as for the top bracket and more than twice as high as for the bracket with rank 11.[16] The foursome of brackets at the lower end

16 A look at the rations of tax share/income share helps to indicate the extent to which the bottom bracket leads the next three income brackets with regard to this measure of disproportionality.

	this case (IV)	reference case (I)
Group of 4 lowest income brackets	121%	87%
Bottom income bracket	163%	116%
Group of next 3 income brackets ($2,000 to $4,999)	114%	82%

TABLE 6

RANK SHIFTING

Total Tax Rates Based on A.G.I.
Comparisons with Reference Case

Decrease in Rate Rank				Increase of Rate Rank		
Column From Col. To Col.	Income Bracket	From	To	Income Bracket	From	To
(1) to (2)	$6000 - 6999 $7000 - 7999	8 7	10 9	$5000 - 5999	11	7
(1) to (3)				$5000 - 5999	11	7
(1) to (4)	$7000 - 7999	7	9	$2000 - 2999 $4000 - 4999	5 4	3 2
	$15,000 and over	1	7	$5000 - 5999	11	6

of the income scale occupies ranks 1 through 3, and 5. However, the rate difference between ranks 4 and 5 being negligible, the four lowest income brackets are situated among the highest rates. This is in consonance with our previous observation that both the extensive shifting assumption and the adjustment serve to move these brackets toward the higher rate ranks. In contrast, the top income bracket has moved from rank 1 to rank 7, and its 11% rate is less than both the overall average (12%) and the immediately preceding $10,000-$14,999 bracket rate (13%).

F. SUMMARY

1. Similarity of the Distributions

The four sets of tax/income ratio calculations presented in columns 1 through 4 of Table 4 appear to yield a broadly similar pattern of results. In general, the group of middle income brackets ($5,000 to $9,999) has the lowest rate assignments, and the five brackets in this group have rather equal rates. The relatively high average effective rate assignment to the bottom income bracket occurs throughout the four sets of estimates. Furthermore, this rate is outstanding in that there is a noticeable difference between the bottom bracket rate and (a) the next highest rate (except in case (2)), and (b) the rates assigned to the other income brackets in the lower income range.

2. Differences in the Distributions

We shall now consider two methods of summarizing the effect (upon the structure of rate estimates) of changing the shifting assumption and/or of introducing the adjustment. Table 6 shows the instances of rank shifts of 2 ranks or more, where an increase in rank (e.g., from rank 11 to rank 7) refers to movement from a lower to a higher estimated tax rate.

We may also examine rate structure change, that is, the pattern of rate changes which results from a change in the basis of calculation. The three columns in Table 7 show the results of comparison of the reference case with each of the other three cases. Each

TABLE 7

Total Tax Rates Based on A.G.I.
Comparisons with Reference Case

Income Bracket	Table 4 Columns		
	(1) vs. (2)	(1) vs. (3)	(1) vs. (4)
Under $2,000	.53	6.23*	1.84*
$ 2,000 - $ 2,999	.47	4.18*	1.08*
$ 3,000 - $ 3,999	.51	3.08*	.71*
$ 4,000 - $ 4,999	.40	3.36*	8.05*
$ 5,000 - $ 5,999	.27	4.78*	1.33*
$ 6,000 - $ 6,999	.75	1.48*	.10
$ 7,000 - $ 7,999	.84	.94*	.34
$ 8,000 - $ 8,999	.77	1.18*	.22
$ 9,000 - $ 9,999	.75	1.24*	.14
$10,000 - $14,999	.88	.66*	.59
$15,000 and over	1.77	8.40	3.79

The * means that the underlying difference is of opposite sign compared to the average and the other entries in the column.

numerical entry measures relative percentage change in tax rate.[17]

Consider column 1 as an example. All the entries except the last are less than 1. A number greater than 1 indicates that under the conservative shifting assumption, the change from "without the adjustment" to "with the adjustment" has a greater effect (in terms of relative percentage change) on the tax rate for the income bracket than on the rate for the overall total (i.e., over all income brackets). Similarly, an entry which is less than 1 indicates a less than average effect. In column 1 the effect for each bracket and for the average is in the same direction, and all underlying changes are positive (that is, for each bracket the rate calculated without the adjustment is higher than the rate with the adjustment). Only the top income bracket has an entry greater than 1 and this bracket may be designated as "G" to signify that its rate fell more than the average did as a result of the application of the adjustment, and the other brackets are designated as "L"[18]

The same brackets appear as "L" in column 2, where the comparison is between the conservative and the extensive shifting assumptions, both without the adjustment. In this

17 For example, the first entry in column 1 is .53. This is calculated from Table 4 as follows: (1) Find the absolute difference between rates in columns 1 and 2 for that bracket. (2) Express the absolute difference and a percentage of the reference case rate. (3) Repeat steps (1) and (2) using the overall average rates. (4) Express the percentage change in step (2) as a ratio to the percentage change in step (4). The relative percentage change measure is used in order to show the percentage change in rate for a bracket, relative to some standard (that is, relative to the overall average).

18 The term "L" is to be interpreted in the following sense: Compared to the where the adjustment is not applied, a change to calculations made with the adjustment will result in a less than average percentage decrease in the "L" bracket's tax rate (a "G" bracket will show a greater than average percentage decrease in its tax rate).

case however, except for the top income bracket and the overall average, all of the underlying changes are negative (that is, for each bracket, except $15,000 and over, the rate calculated for the extensive shifting assumption exceeds the rate for the conservative assumption).

In the sense that the direction of the effect is not the same for all brackets, the effect in the "change in shifting assumptions" case may be considered to be more severe than that in the "without the adjustment—with the adjustment" case. Furthermore, a difference between the two cases may be noted with respect to the inter-bracket distribution of the effect on the members of the "L" group. In column 2, there is a positive relation between the magnitude of the effect and the absolute size of the number in the etryn whereas in column 1 this relation is negative. Keeping this in mind, we note that there is a difference between the two cases with respect to the relative magnitude of each effect on a given income bracket. The bottommost income bracket, for example, is affected to a relatively greater degree by the change in shifting assumption than by the application of the adjustment, whereas the opposite is true for the $7,000–$7,999 bracket.

The entries in column 3 show the effect of the change from the conservative shifting assumption without the adjustment to the extensive shifting assumption with the adjustment. Once again the only member of the "G" set is the top income bracket. The five income brackets between $6,000 and $14,999 show changes in the same direction as the top bracket, but because these changes —which are positive—are all less than the overall average, these five brackets are again members of the "L" set. The other members of the "L" set, the five brackets of less than $6,000 income, all show an underlying change which is negative and therefore opposite in direction to the average.

IV. AVERAGE EFFECTIVE TOTAL TAX RATES BASED ON OTHER INCOME CONCEPTS

Thus far we have dealt with average effective rate estimates based on A.G.I., and now attention will be turned to rates based on other income concepts. Table 8 is similar to Table 4 except that the rates refer to A.G.I. Minus Federal Tax Payments. Similarly we have Tables 9 and 10 which show rate estimates based on Broadened Income and Broadened Income Minus Federal Tax Payments respectively.[19]

Rather than go through as detailed a review of the results as we have for A.G.I., our attention will be directed to the effect upon the rate structure due to a change in income

19 Space limitations for this paper do not permit the inclusion of details of the method and reasoning underlying the calculations but these are available on request. The additions to A.G.I. for Broadened Income include government transfer payments, undistributed corporate profits, unshifted corporate income tax, employers' contribution of social security, unemployment insurance, and undistributed fiduciary income. The federal tax payment deductions from both A.G.I. and Broadened Income include personal and the forward shifted portion of corporate income tax, employee's contribution to social security excise, gift, and estate taxes, the employer's contribution to social security and the unshifted portion of corporate income tax.

TABLE 8

Total Tax: Average Effective Tax Rate By Income Bracket
(Based on Adjusted Gross Income minus Fed. Tax)

Income Bracket	(1) Conservative Shifting Assumption without Adjustment		(2) Conservative Shifting Assumption with Adjustment		(3) Extensive Shifting Assumption without Adjustment		(4) Extensive Shifting Assumption with Adjustment	
	Percent	Rank	Percent	Rank	Percent	Rank	Percent	Rank
Under $ 2000	20.85	2	17.68	2	29.94	1	29.21	1
$ 2000 - $ 2999	14.32	5	12.37	5	18.20	5	17.51	3
$ 3000 - $ 3999	13.87	6	11.80	6	16.67	6	15.98	5
$ 4000 - $ 4999	15.04	4	13.29	4	18.33	4	17.59	2
$ 5000 - $ 5999	11.88	11	10.94	7	15.40	7	14.93	7
$ 6000 - $ 6999	13.08	9	10.23	10	14.54	9	13.25	8
$ 7000 - $ 7999	13.58	7	10.27	9	14.70	8	13.23	9
$ 8000 - $ 8999	12.43	10	9.66	11	13.57	11	12.31	11
$ 9000 - $ 9999	13.10	8	10.28	8	14.37	10	13.18	10
$10000 - $14999	17.88	3	13.34	3	19.25	3	16.78	4
$15,000 and over	40.70	1	19.86	1	23.08	2	15.92	6
Overall total	18.16	(2-3)	12.90	(4-5)	17.78	(5-6)	15.71	(6)

TABLE 9

Total Tax: Average Effective Tax Rate By Income Bracket
(Based on Broadened Inc.)

Income Bracket	(1) Conservative Shifting Assumption without Adjustment		(2) Conservative Shifting Assumption with Adjustment		(3) Extensive Shifting Assumption without Adjustment		(4) Extensive Shifting Assumption with Adjustment	
	Percent	Rank	Percent	Rank	Percent	Rank	Percent	Rank
Under $ 2000	12.27	3	10.40	1	16.60	1	16.20	1
$ 2000 - $ 2999	8.08	11	6.97	11	9.96	11	9.58	9
$ 3000 - $ 3999	9.36	9	7.97	6	11.01	6	10.56	5
$ 4000 - $ 4999	10.74	4	9.50	3	12.77	3	12.26	2
$ 5000 - $ 5999	9.12	10	8.40	5	11.49	4	11.15	4
$ 6000 - $ 6999	9.75	7	7.63	8	10.66	9	9.72	7
$ 7000 - $ 7999	10.08	5	7.62	9	10.76	8	9.68	8
$ 8000 - $ 8999	9.58	8	7.45	10	10.32	10	9.36	10
$ 9000 - $ 9999	10.04	6	7.88	7	10.84	7	9.94	6
$10000 - $14999	13.03	2	9.72	2	13.74	2	11.98	3
$15,000 and over	19.26	1	9.40	4	11.43	5	7.88	11
Overall total	12.15	(3)	8.64	(5)	11.79	(4)	10.41	(5)

TABLE 10

Total Tax: Average Effective Tax Rate By Income Bracket
(Based on Broadened Inc. minus Fed. Tax)

Income Bracket	(1) Conservative Shifting Assumption without Adjustment		(2) Conservative Shifting Assumption with Adjustment		(3) Extensive Shifting Assumption without Adjustment		(4) Extensive Shifting Assumption with Adjustment	
	Percent	Rank	Percent	Rank	Percent	Rank	Percent	Rank
Under $ 2000	15.10	3	12.80	2	21.26	1	20.74	1
$ 2000 - $ 2999	9.55	11	8.24	11	11.98	11	11.53	11
$ 3000 - $ 3999	11.45	9	9.74	7	13.70	7	13.13	5
$ 4000 - $ 4999	13.26	4	11.72	4	16.10	4	15.45	3
$ 5000 - $ 5999	11.01	10	10.13	5	14.23	5	13.80	4
$ 6000 - $ 6999	12.15	7	9.50	9	13.49	9	12.30	9
$ 7000 - $ 7999	12.64	5	9.56	8	13.67	8	12.31	8
$ 8000 - $ 8999	11.94	8	9.28	10	13.04	10	11.83	
$ 9000 - $ 9999	12.52	6	9.82	6	13.72	6	12.58	6
$10000 - $14999	17.02	2	12.70	3	18.32	2	15.97	2
$15,000 and over	31.50	1	15.38	1	17.88	3	12.33	7
Overall total	15.86	(2-3)	11.27	(4)	15.50	(4-5)	13.69	(4)

concept. We will look first at the patterns of rank shifts and then at the patterns of rate structure changes.

A. RANK SHIFTS

To consider the effect of deducting federal tax payments, compare the ranks in a given column for Table 4 v.s. Table 8 for A.G.I., and for Table 9 v.s. Table 10 for Broadened Income. We conclude that there is not much effect on the pattern of ranks due to a change from income to income after federal tax payments, whether we use A.G.I. or Broadened Income. This holds for both shifting assumptions, with and without the adjustment.

The effect of the change from A.G.I. to "Broadened Income" is somewhat more complex. Table 11 shows the increases of rank shifts of 2 ranks or more.

Generally, with respect to ranks, a change from A.G.I. to Broadened Income mainly moves the $2,000–$2,999 bracket to lower ranks and moves the brackets $9,000–$9,999 to higher ranks.

B. RATE STRUCTURE CHANGES

We may now look at rate structure change in terms of the relative percentage measure. We conclude that the effect of a change from A.G.I. to any of the other three income concepts is independent of whether the rate calculations include the adjustment or not.[20] Table 12 shows the distributions of relative percentage change (based on rates calculated without the adjustment).

20 This is because the distributions of relative percentage change figures turn out to be virtually invariant with respect to the adjustment.

TABLE II

RANK SHIFTING

Total Tax Rates Based on Various Income Concepts

	Decrease in Rate Rank						Increase in Rate Rank					
	A.G.I. v.s. B.I.			A.G.I.* v.s. B.I.*			A.G.I. v.s. B.I.			A.G.I.* v.s. B.I.*		
		Rank Shift			Rank Shift			Rank Shift			Rank Shift	
	Bracket	From	To	Bracket	From	To	Bracket	From	To	Bracket	From	To
Conservative Shifting Assumption Without Adjustment	$2000-2999	5	11	$2000-2999	5	11	$7000-7999	7	5	$6000-6999	9	7
	$3000-3999	6	9	$3000-3999	6	9	$8000-8999	10	8	$7000-7999	7	5
							$9000-9999	9	6	$8000-8999	10	8
Conservative Shifting Assumption With Adjustment	$2000-2999	5	11	$2000-2999	5	11	$5000-5999	7	5	$5000-5999	7	5
							$6000-6999	10	8	$9000-9999	8	5
	$15,000 and over	2	4				$10000-14999	4	8			
Extensive Shifting Assumption Without Adjustment	$2000-2999	5	11	$2000-2999	5	11	$5000-5999	7	4	$5000-5999	7	5
	$15,000 and over	2	5				$9000-9999	10	7	$9000-9999	10	6
Extensive Shifting Assumption With Adjustment	$2000-2999	3	9	$2000-2999	3	11	$5000-5999	6	4	$5000-5999	7	4
	$15,000 and over	7	11				$9000-9999	10	6	$9000-9999	10	6
										$10000-14999	4	2

A.G.I. = Adjusted Gross Income
B.I. = Broadened Income
A.G.I.* = Adjusted Gross Income Minus Federal Taxes
B.I.* = Broadened Income Minus Federal Taxes

TABLE 12

RELATIVE PERCENTAGE CHANGE

Total Tax Rates Based on Various Income Concepts

	(1)	(2)	(3)	(4)	(5)	(6)
	A.G.I. vs. Broadened Income		A.G.I. vs. A.G.I. Federal Tax		A.G.I. vs. Broadened Income-Fed. Tax	
Brackets	a.	b.	a.	b.	a.	b.
Under $ 2000	1.59	1.73	.96	1.15	1.61*	.63*
$ 2000 - $ 2999	1.80	2.01	.89	.93	2.69*	1.64*
$ 3000 - $ 3999	1.09	1.18	.86	.86	.18*	.13
$ 4000 - $ 4999	.80	.86	.88	.89	.80	.83
$ 5000 - $ 5999	.51	.56	.80	.82	1.32	1.19
$ 6000 - $ 6999	.63	.64	.83	.83	1.44	1.27
$ 7000 - $ 7999	.64	.63	.85	.85	1.51	1.33
$ 8000 - $ 8999	.46	.45	.83	.82	1.97	1.62
$ 9000 - $ 9999	.49	.48	.84	.83	1.90	1.58
$10000 - $14999	.54	.51	1.05	1.07	2.47	2.10
$15000 and over	1.92	1.85	1.70	1.59	1.03	1.01

a. Conservative Shifting Assumption Without Adjustment
b. Extensive Shifting Assumption Without Adjustment
The * indicates that the underlying difference is of opposite sign compared the average and the other entries in the column.

For column 1, all the underlying changes are positive (that is, the rate for each bracket, based on A.G.I. is higher than the rate based on "Broadened Income"). The brackets which show entries less than 1 are all between $4,000 and $14,999. These brackets may be designated as "L" to signify that their rates fell less than the average did under this income concept change, and the other brackets are designated as "G".[21]

The same brackets appear as "L" in column 2. Some brackets have higher numbers in column 2 than they do in column 1 (e.g., the first bracket, a "G", and the $5,000–$5,999, and "L") and some have lower numbers (e.g., the highest income bracket, a "G", and the $8,000–$8,999, an "L"). But the patterns in columns 1 and 2 are similar and so in general it seems that the rate structure change from A.G.I. to the "Broadened Income" concept is not much influenced by the choice of shifting assumption.

Now the effect of the change from A.G.I. to A.G.I. minus federal taxes paid may be considered by examining columns 3 and 4. The underlying figures show that here the differences are all negative (that is, the rates based on A.G.I. are all lower than the rates for

21 The term "L" is to be interpreted in the following sense: Compared to the case where A.G.I. is considered to be the income concept relevant for the effective tax rate calculation, a change to the "Broadened Income" concept will result in a less than average % decrease in the "L" bracket's tax rate (a "G" bracket will show a greater than average % decrease in its tax rate).

A.G.I. minus federal taxes). Therefore those brackets with numbers less than 1 may be designated as "G" because their rates show a less than average % increase, and the other brackets are designated as "L". In column 3, all brackets except the pair of highest incomes fall into this category. In column 4, the bottom income bracket joins the previous pair of "L" (those brackets with numbers greater than 1, whose rates show a greater than average % increase due to the change in income concept). Except for the lowest and highest income brackets, the numbers in columns 3 and 4 are quite similar, and this indicates that, except at the income extremes, the rate structure change due to this change in income concept is not much influenced by the choice of shifting assumption. However, the bottom bracket fares rather differently[22] under the conservative shifting assumption than it does under the more extensive one, from the point of view of the effect which this change in income concept has on the % change in the bracket's tax rate compared to the average. This bracket is a "G" under the conservative and an "L" under the more extensive shifting assumption. The highest income bracket is an "L" under both assumptions, but to a lesser extent under the extensive than with the conservative shifting assumption. This is because of the effect which the choice of shifting assumption has on the estimates of the federal tax payments by brackets (a big item here is the excise tax component). The fact the highest bracket shows up as an "L" is not surprising, given the importance and progressivity of federal income taxes.

Finally, the effect of the change from A.G.I. to Broadened Income minus federal taxes paid may be considered by examining columns 5 and 6. For column 5 the underlying differences are all negative except for the first three brackets (which bear asterisks). These brackets are designated as "G" because their tax rates decrease as a result of this change in income concept. The only other "G" is the $4,000–$4,999 bracket (the entry is less than 1). Much the same is true in column 10 on this score, except that only the first 2 brackets have positive underlying differences. Again only the first 4 brackets are "G".

In comparing columns 5 and 6 to get an indication of whether the shifting assumption influences the effect of the change in income concept, the following is noted. The first two brackets show rather large differences (their change is lower under the more extensive shifting assumption, and this is because the impact of the assumption change is relatively stronger with respect to the federal income taxes deduction than with respect to the income broadening additions, for these brackets). The entries for the other brackets show much less inter-column variation, but column 5 entries are generally higher, the difference is small for the $3,000 to $3,999 bracket, and the difference gets larger over the range of brackets to $14,999, with the highest income bracket showing a small inter-column difference.

In summary the following may be noted.

a. Lower income bracket rates (under $4,000) are relatively low under A.G.I., in the sense that they are among the "G" brackets (their rates increase more or decrease less than the average, in % terms) in each case of change in income concept considered here.

b. The pair of highest income brackets show a rather opposite pattern. With a single exception (the top income bracket in the change to Broadened Income) they are always among the "L" brackets. Thus their rates are

22 A member of this bracket might interpret this to mean "fares better".

relatively high under A.G.I. (in the same relative sense as indicated above). The group of middle income brackets are among the "G" brackets with the change to A.G.I. minus federal taxes, and among the "L" brackets in the other cases.

V. AVERAGE EFFECTIVE COMPONENT TAX RATES

At this point we turn to the average effective tax rate calculations for the four major component taxes.[22a] also shown in Graph 3. We again note a rather "U" shaped rate structure, in which the right-hand extremity (top income bracket) at 12% lies noticeably above the left (bottom bracket) at 9%. The brackets from $2,000 through $9,999 form a more or less flat bottom at about 4% (i.e., relative proportionality at a relatively low rate).[23] Although this pattern

A. EXCISE TAX

Table 13 deals with the general excise tax, and the format is identical to Table 4. Column 1 again presents the reference case. The reference case for the general excise is

22a The discussion involves only the estimates based on A.G.I. because our analysis (similar to that in Section IV.) indicates that the rate patterns are relatively insensitive to the choice of income concept.

23 We are aware that for a given absolute rate difference, the percentage difference is larger for a component tax than for overall total taxes. However, we prefer to be cautious about the significance of rate differences in view of rather imprecise data and estimating procedures.

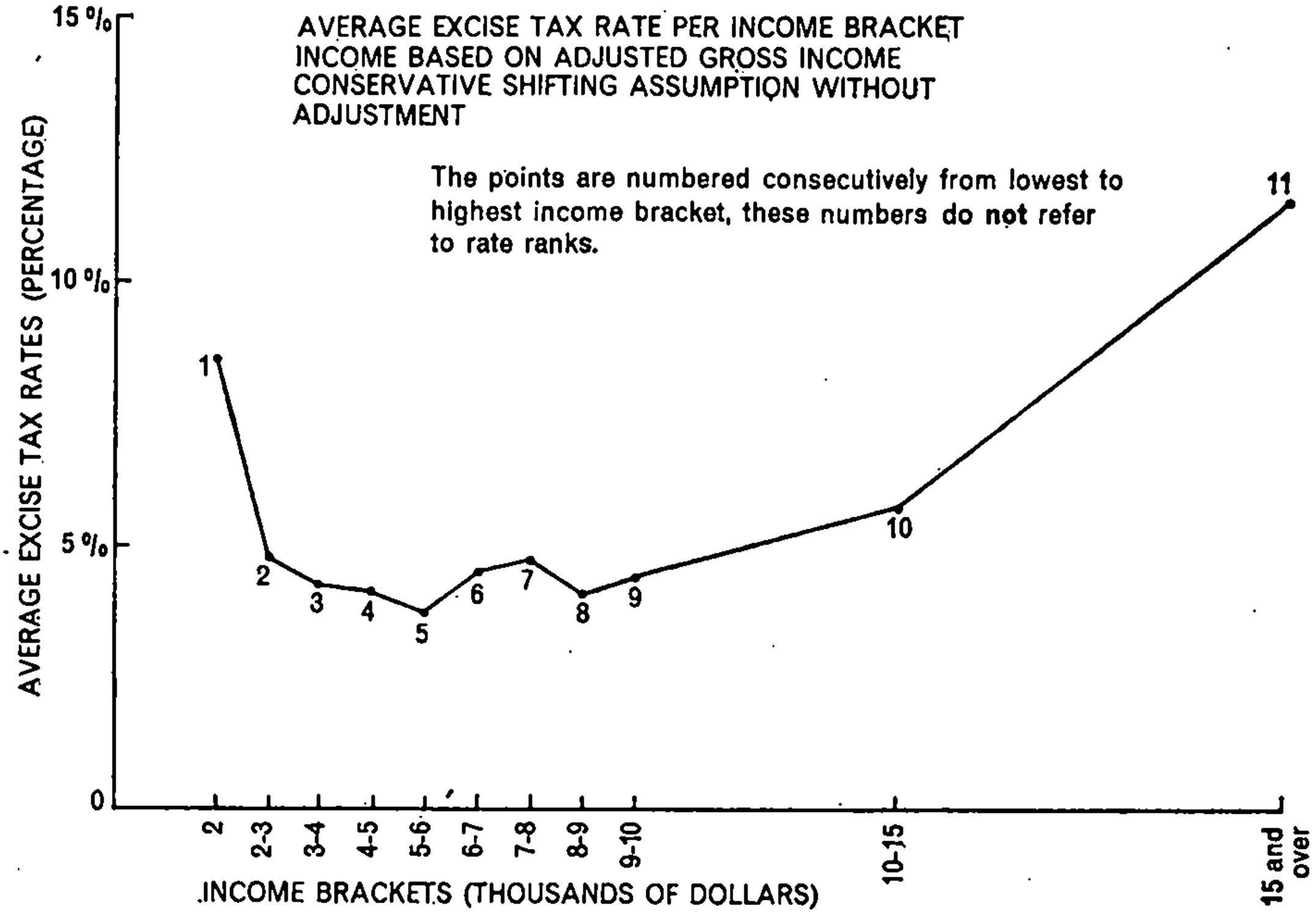
TABLE 13

EXCISE TAX

Average Effective Rates Based on A.G.I.

Income Bracket	(1) Conservative Shifting Assumption w/o Adjust.		(2) Conservative Shifting Assumption with Adjust.		(3) Extensive Shifting Assumption w/o Adjust.		(4) Extensive Shifting Assumption with Adjust.	
	Percent	Rank	Percent	Rank	Percent	Rank	Percent	Rank
Under $ 2000	8.61	2	7.42	1	11.05	1	10.82	1
$ 2000 - $ 2999	4.62	4	3.92	4	5.82	3	5.62	2
$ 3000 - $ 3999	4.12	8	3.36	9	4.92	6	4.71	6
$ 4000 - $ 4999	4.03	9	3.41	6	5.00	5	4.80	4
$ 5000 - $ 5999	3.69	11	3.37	8	4.85	7	4.72	5
$ 6000 - $ 6999	4.41	6	3.39	7	4.73	9	4.40	7
$ 7000 - $ 7999	4.60	5	3.42	5	4.79	8	4.40	8
$ 8000 - $ 8999	4.00	10	3.01	11	4.27	11	3.93	11
$ 9000 - $ 9999	4.28	7	3.28	10	4.59	10	4.26	10
$10000 - $14999	5.70	3	4.23	3	5.94	2	5.39	3
$15000 and over	11.53	1	5.24	2	5.80	4	4.27	9
OVERALL	5.76	3	3.96	4	5.41	4-5	4.90	4

GRAPH 3



GRAPH 4

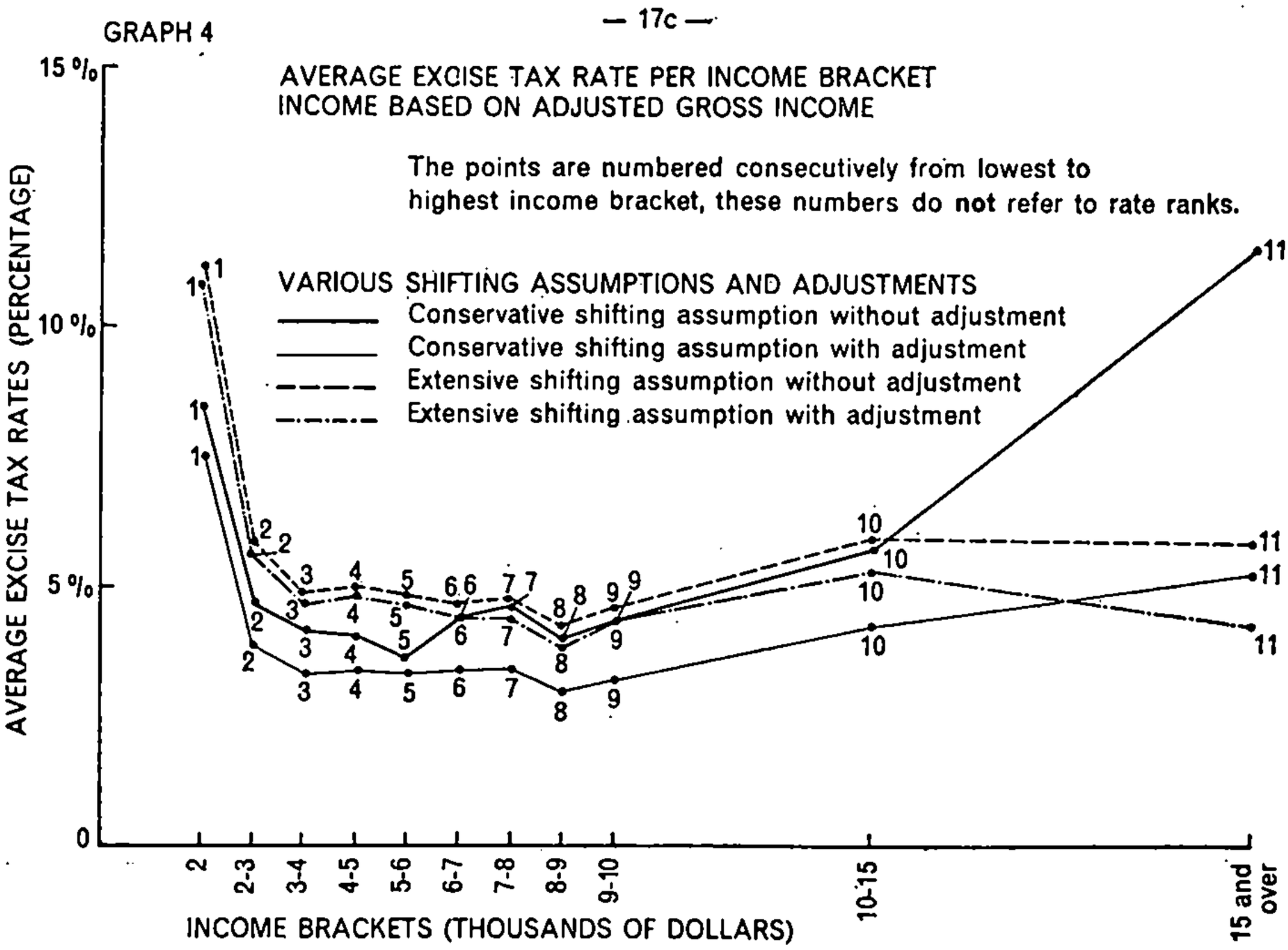


TABLE 14

PERSONAL INCOME TAX

Average Effective Rates Based on A.G.I.

Income Bracket	(5) Conservative Shifting Assumption w/o Adjust.		(6) Conservative Shifting Assumption with Adjust.	
	Percent	Rank	Percent	Rank
Under $ 2000	1.29	11	1.28	11
$ 2000 - $ 2999	2.02	10	1.96	10
$ 3000 - $ 3999	2.24	9	2.17	9
$ 4000 - $ 4999	2.33	8	2.22	8
$ 5000 - $ 5999	2.48	7	2.39	5
$ 6000 - $ 6999	2.58	5-6	2.35	6
$ 7000 - $ 7999	2.58	5-6	2.33	7
$ 8000 - $ 8999	2.86	3-4	2.60	4
$ 9000 - $ 9999	2.86	3-4	2.64	3
$10000 - $14999	3.30	2	2.78	2
$15000 and over	4.36	1	3.19	1
OVERALL	2.88	3-4	2.51	4-5

of rates is similar to the results obtained for the tax structure as a whole, the lowest rate situations for the excise tax are not limited to the middle income group. The rates range from about 11½% to about 3½%, and the overall average rate is about 5.7%. This is of interest, since the maximum nominal rate on any single transaction was 3½% ad valorem.[24] In Graph 4 the line of heavy solid segments repeats the reference case, and the other three lines show the information in columns 2, 3, and 4 of Table 13. The line of light solid segments represents the case where the adjustment is considered with the conservative shifting assumption (see column 2). The entire curve is shifted down relative to the reference case. The lowest income bracket has the highest rate, and bracket numbers 10 and 11 have rates slightly above the "floor". The situation is similar to the analogous case for the tax structure as a whole.

The line shows the rates based on the extensive shifting assumption, without the adjustment (see column 3 of Table 13). There is significant modification of the reference case; in particular there is really no right arm to the "U". Bracket numbers 2, 10, and 11 lie slightly above the floor (at 5%) and the bottom bracket is perched high above all (at 11%). Again the situation resembles the analogous case for total taxes.

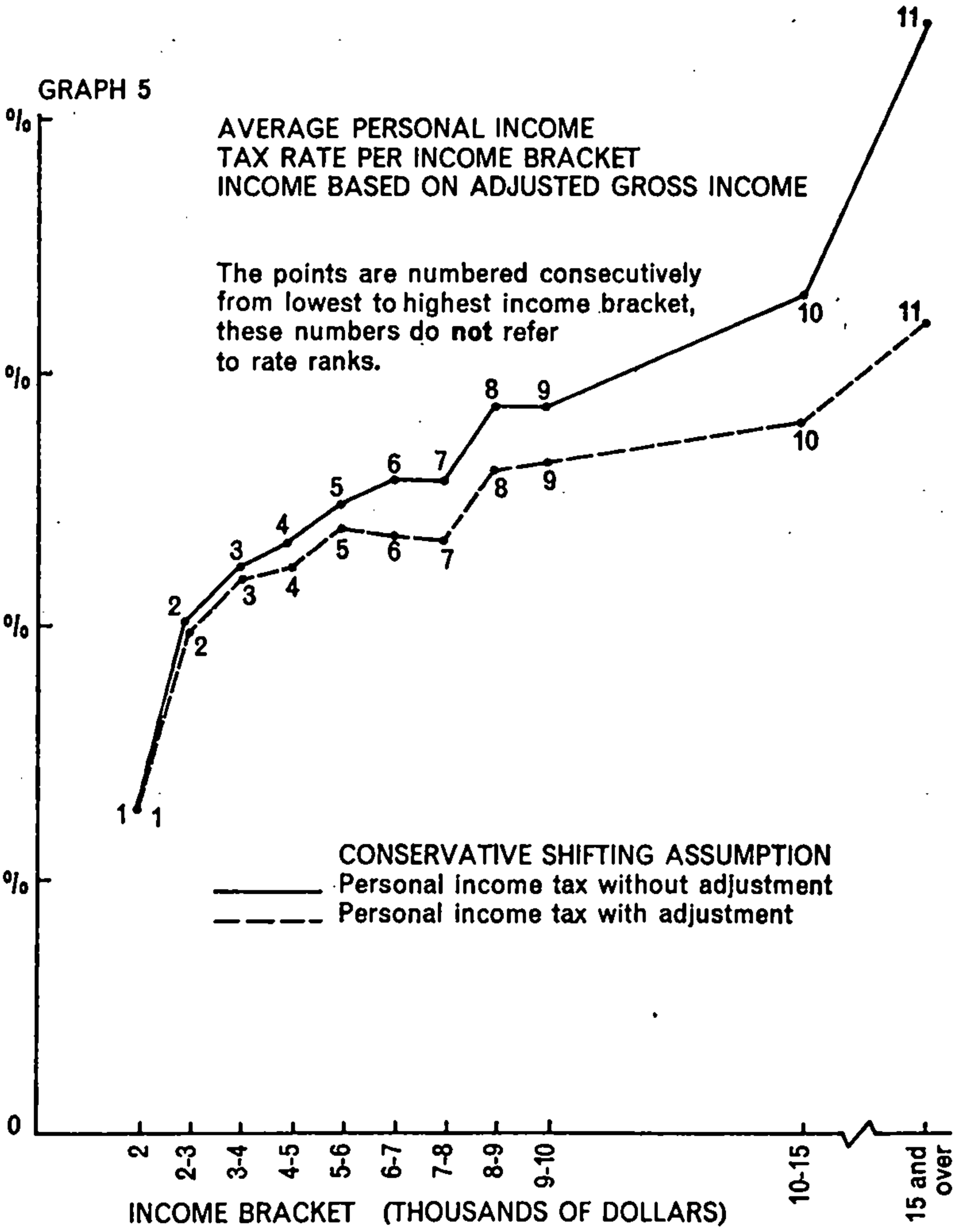
24 It has been suggested that the explanation of the inter-bracket variation in the ratio: excise tax assignment/income is to be found in the inter-bracket variation in proportion of income spent on taxable items. However, this is insufficient in the case of a multistage tax such as the general excise which applies at every level of production and distribution, even if all nominal tax rates are the same and the hypothesis of 100% forward shifting is maintained. This subject is treated in the author's "Some Analysis Concerning the Regressivity of the Hawaii General Excise," National Tax Journal, June, 1965.

The line illustrates the extensive shifting assumption with the adjustment (see column 4). As compared to the reference case, the top income bracket shows a noticeable rate decrease (at 4% it is below average and has rank 9). The bottom bracket rate of 11% is outstanding, and the $2,000–$2,999 bracket has moved to rank 2. Again these results are similar to what was found for the tax structure as a whole.

B. INCOME TAX

Turning now to the personal income tax, we may examine Table 14. The assumption of zero shifting was maintained and so there are only a pair of cases for comparison, with and without adjustment. Graph 5 depicts the situation. The reference case shows a progressive effective rate structure, with relatively more progression at either end of the income scale than in the middle. Recognition of the

GRAPH 5



adjustment results in only a slight rate reduction for the lower income brackets (say, up through $4,999). However, for the higher brackets a rate reduction occurs which is both noticeable and increasing with income.[25]

C. PROPERTY TAX

The distributions of rate estimates for the property tax appear in Table 15 and in Graphs 6 and 7. Again, the reference case has a rough "U" shape; however, the "floor" has a noticeable downward slope, with most of the regression located in the area of the pair of lowest income brackets.

When the adjustment is introduced with the conservative shifting assumption, all rates are lower than in the reference case. Again the highest rates are at the extreme ends of the income scale, but now the bottom and next-to-the-bottom brackets rank 1 and 3; and the top and next-to-the-top brackets rank 2 and 4 respectively. The rate spread between the former pair indicates regression whereas between the latter pair there is an area of progression.

With the extensive shifting assumption without adjustment, all rates except that of the top income bracket are higher than in the reference case. The first five brackets all have higher ranks than in the reference case,

25 This is understandable, given the progressivity of the federal personal income tax. Note also the minor breaks in the upward slope of the line, which indicate lapses in progression.

TABLE 15

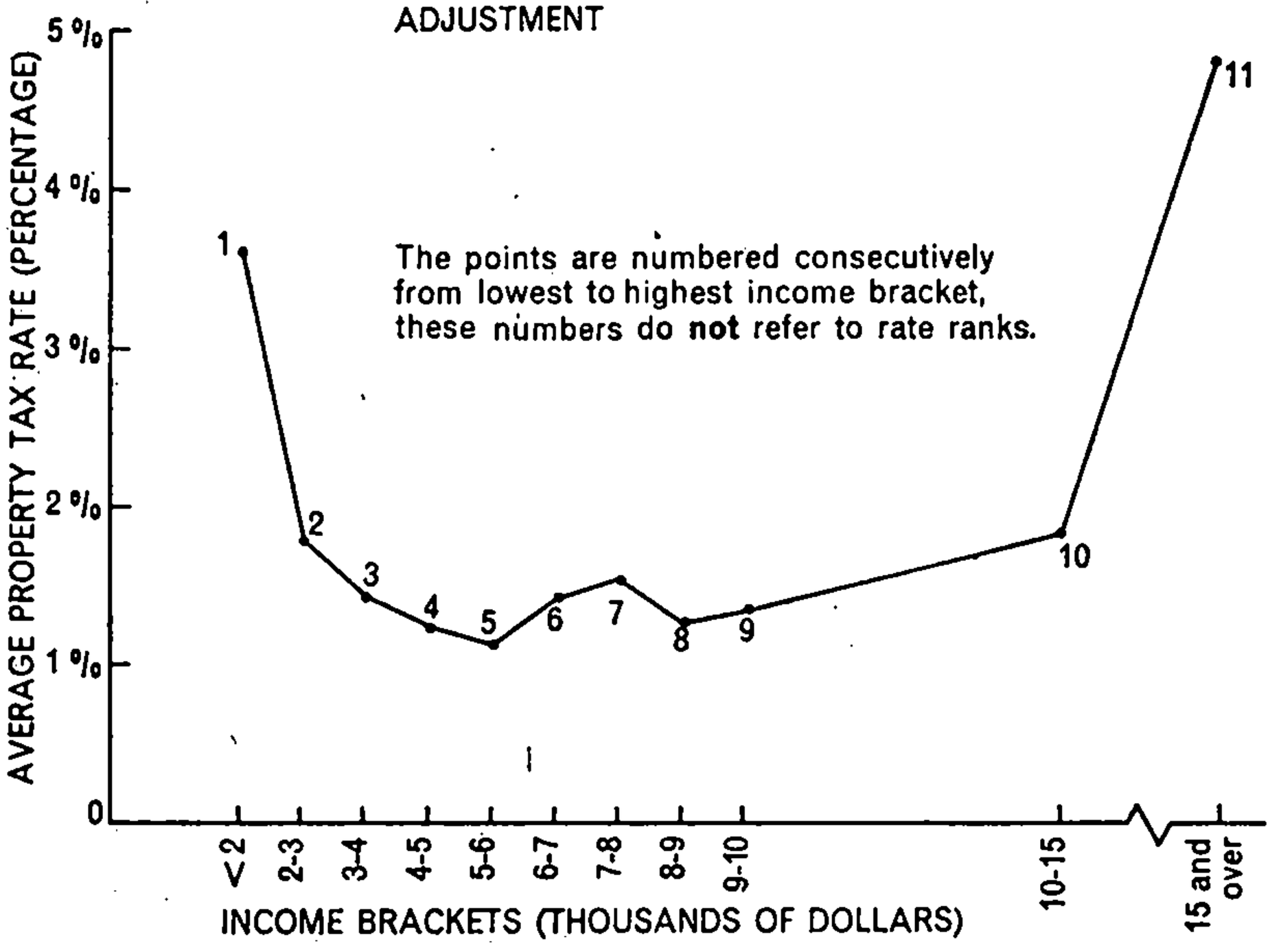
PROPERTY TAX

Average Effective Rates Based on A.G.I.

Income Bracket	(7) Conservative Shifting Assumption w/o Adjust		(8) Conservative Shifting Assumption with Adjust.		(9) Extensive Shifting Assumption w/o Adjust.		(10) Extensive Shifting Assumption with Adjust.	
	Percent	Rank	Percent	Rank	Percent	Rank	Percent	Rank
Under $ 2000	3.66	2	3.09	1	5.25	1	5.13	1
$ 2000 - $ 2999	1.79	4	1.46	3	2.53	2	2.40	2
$ 3000 - $ 3999	1.46	6	1.12	5	1.98	4	1.87	3
$ 4000 - $ 4999	1.22	10	0.95	10	1.83	6	1.71	4
$ 5000 - $ 5999	1.14	11	0.98	7	1.76	7	1.68	5
$ 6000 - $ 6999	1.41	7	0.97	8	1.59	9	1.40	8
$ 7000 - $ 7999	1.53	5	1.03	6	1.67	8	1.44	7
$ 8000 - $ 8999	1.29	9	0.88	11	1.47	11	1.29	10
$ 9000 - $ 9999	1.38	8	0.96	9	1.58	10	1.40	9
$10000 - $14999	1.80	3	1.17	4	1.91	5	1.54	6
$15000 and over	4.84	1	2.20	2	2.12	3	1.25	11
OVERALL	2.07	3	1.31	3-4	1.98	4	1.68	5

GRAPH 6

AVERAGE PROPERTY TAX RATE PER INCOME BRACKET
INCOME BASED ON ADJUSTED GROSS INCOME
CONSERVATIVE SHIFTING ASSUMPTION WITHOUT ADJUSTMENT



GRAPH 7

AVERAGE PROPERTY TAX RATE PER INCOME BRACKET
INCOME BASED ON ADJUSTED GROSS INCOME

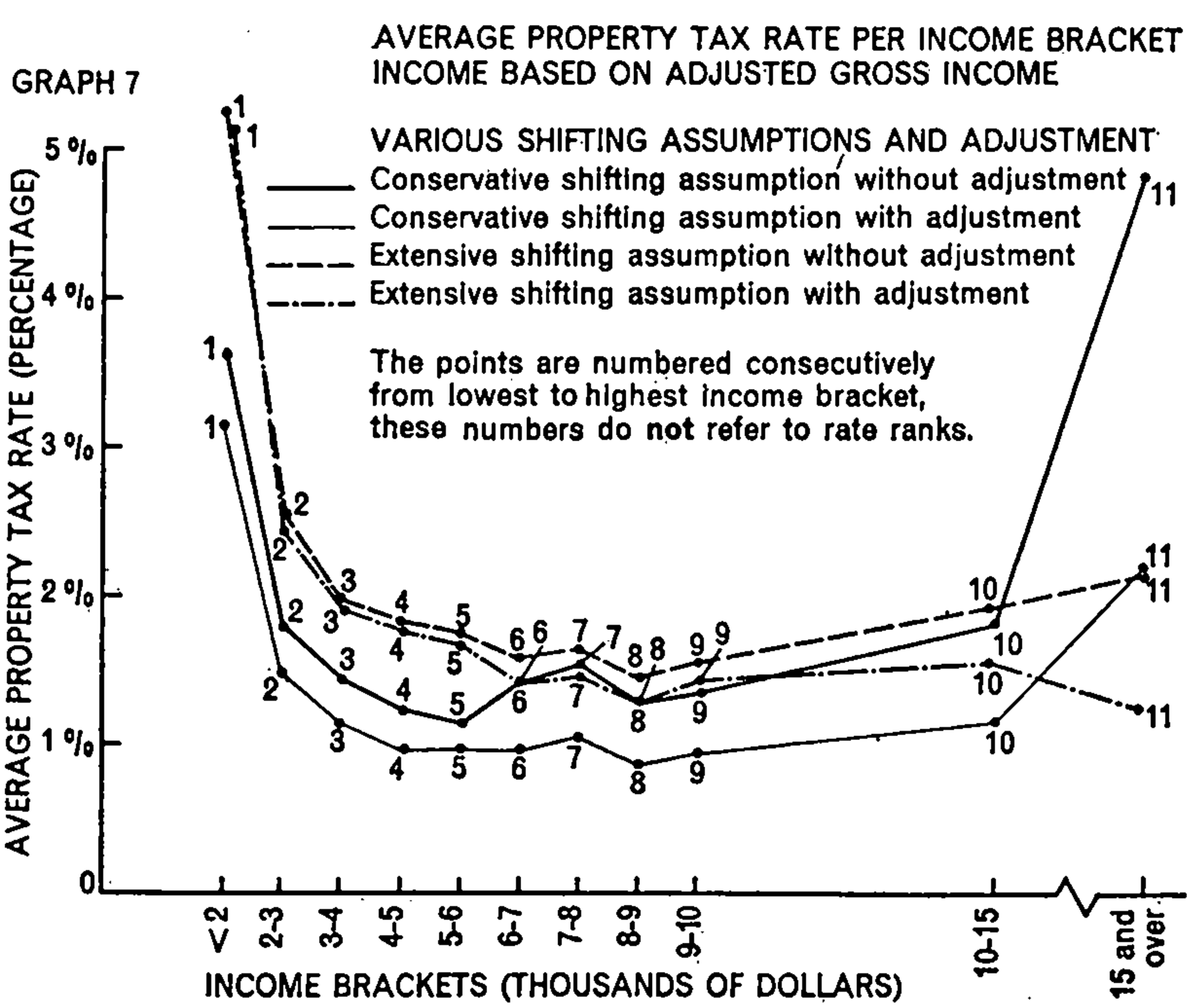


TABLE 16

FUEL TAX

Average Effective Rates Based on A.G.I.

Income Bracket	(11) Conservative Shifting Assumption w/o Adjust.		(12) Conservative Shifting Assumption with Adjust.		(13) Extensive Shifting Assumption w/o Adjust.		(14) Extensive Shifting Assumption with Adjust.	
	Percent	Rank	Percent	Rank	Percent	Rank	Percent	Rank
Under $ 2000	0.98	11	0.52	11	2.17	1	2.16	1
$ 2000 - $ 2999	1.16	8	0.84	9	1.60	6	1.55	5
$ 3000 - $ 3999	1.01	10	0.69	10	1.41	9	1.36	9
$ 4000 - $ 4999	1.26	7	0.98	5	1.69	4	1.61	3
$ 5000 - $ 5999	1.07	9	0.91	7	1.57	7	1.52	6
$ 6000 - $ 6999	1.49	3	1.05	3	1.72	3	1.57	4
$ 7000 - $ 7999	1.48	4	0.99	4	1.63	5	1.47	7
$ 8000 - $ 8999	1.27	6	0.86	8	1.38	10	1.25	10
$ 9000 - $ 9999	1.37	5	0.94	6	1.48	8	1.37	8
$10000 - $14999	1.96	2	1.28	2	1.97	2	1.66	2
$15000 and over	4.90	1	2.13	1	1.32	11	0.97	11
OVERALL	1.94	2	1.15	2-3	1.62	6	1.45	6

whereas all other brackets have lower ranks, thus showing the differential impact of the change in shifting assumption.[26]

When the adjustment is combined with the extensive shifting assumption we get a picture similar to the one just discussed. In particular we note that the top income bracket has the lowest rate of all, and the five highest ranks are occupied by the five lowest income brackets. In this gross sense, then, the rate structure is regressive.

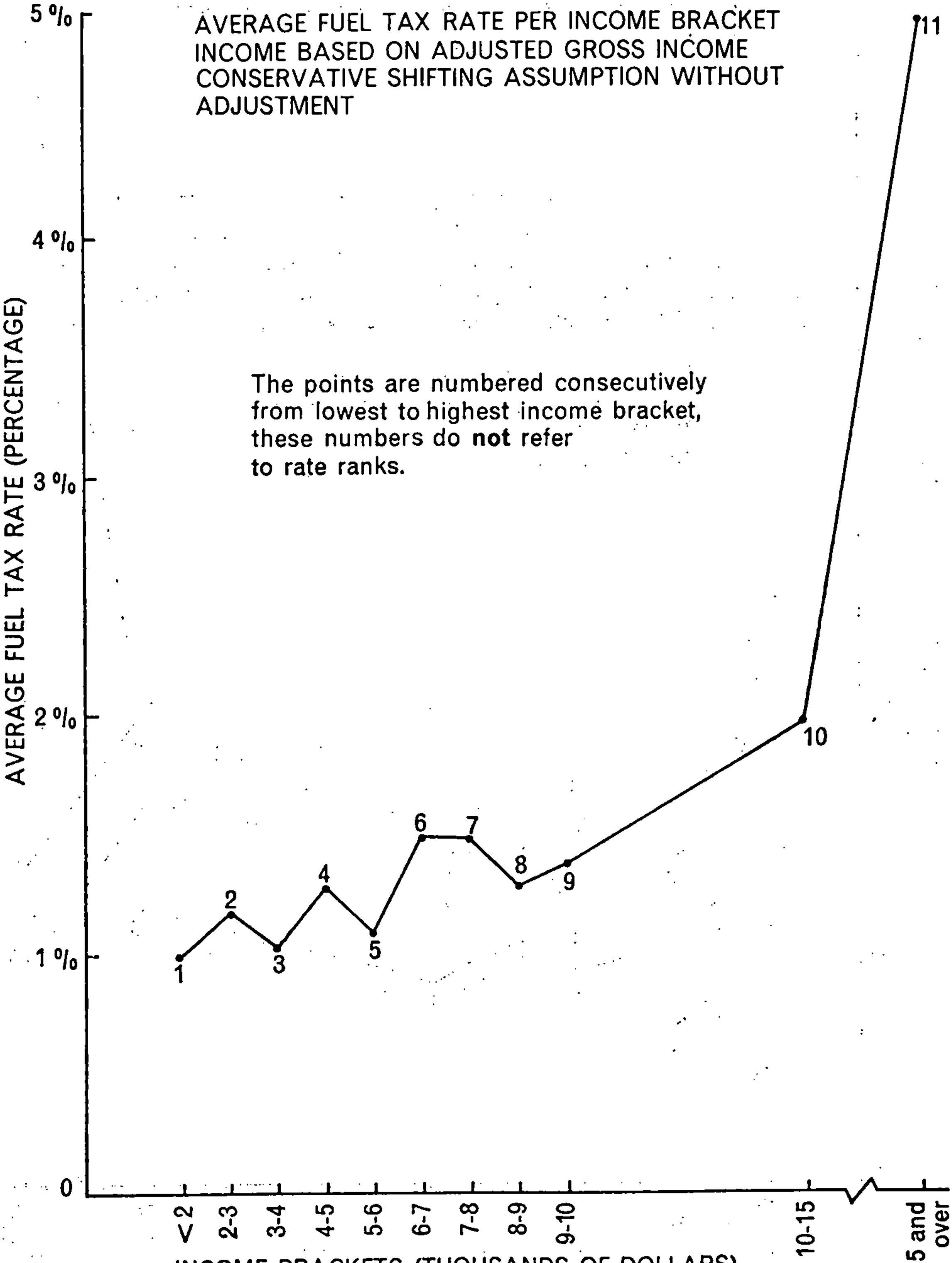
D. FUEL TAX

The last component to be examined here is the fuel tax. The rate distributions are shown in Table 16 and in Graphs 8 and 9. For the reference case the rate structure shows progression which is mild through incomes up to $10,000, and increases for higher incomes, but the progressivity is less pronounced than for the income tax.[27] The conservative assumption with adjustment case shows lower rates, especially for the highest income

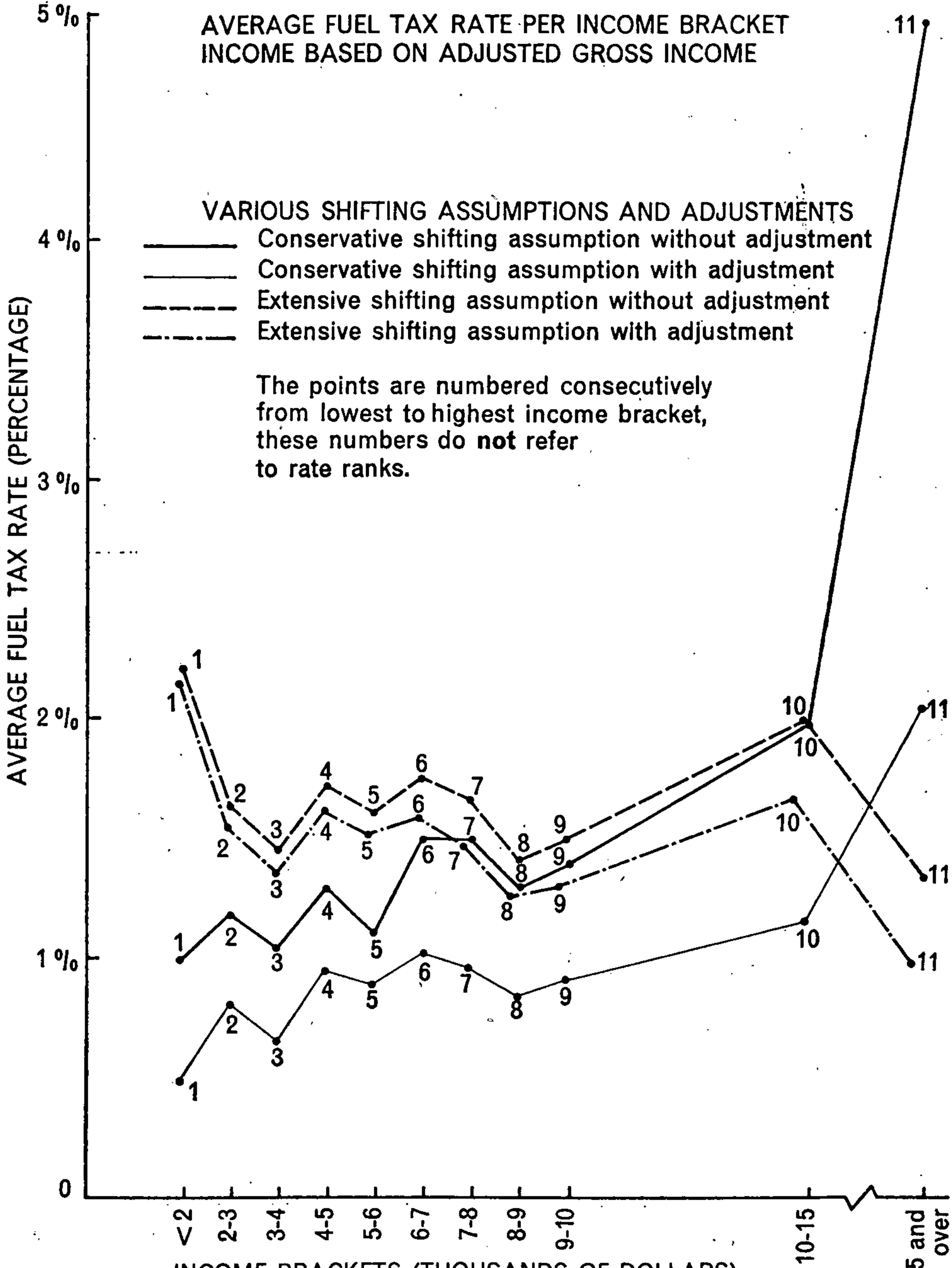
26 This is understandable because the lower income groups are more likely to be tenants than landlords and to be more effected by the impact on use rather than source of income (the opposite is suggested for the higher income brackets).

27. The patterns of source and use of income which account for these estimates will not be discussed here.

GRAPH 8


AVERAGE FUEL TAX RATE PER INCOME BRACKET
INCOME BASED ON ADJUSTED GROSS INCOME
CONSERVATIVE SHIFTING ASSUMPTION WITHOUT ADJUSTMENT
The points are numbered consecutively from lowest to highest income bracket, these numbers do **not** refer to rate ranks.
AVERAGE FUEL TAX RATE (PERCENTAGE)
5 %
4 %
3 %
2 %
1 %
0
1
2
3
4
5
6
7
8
9
10
11
<2
2-3
3-4
4-5
5-6
6-7
7-8
8-9
9-10
10-15
15 and over
INCOME BRACKETS (THOUSANDS OF DOLLARS)

GRAPH 9


AVERAGE FUEL TAX RATE PER INCOME BRACKET
INCOME BASED ON ADJUSTED GROSS INCOME
VARIOUS SHIFTING ASSUMPTIONS AND ADJUSTMENTS
Conservative shifting assumption without adjustment
Conservative shifting assumption with adjustment
Extensive shifting assumption without adjustment
Extensive shifting assumption with adjustment
The points are numbered consecutively from lowest to highest income bracket, these numbers do not refer to rate ranks.
AVERAGE FUEL TAX RATE (PERCENTAGE)
5 %
4 %
3 %
2 %
1 %
0
< 2
2-3
3-4
4-5
5-6
6-7
7-8
8-9
9-10
10-15
15 and over
INCOME BRACKETS (THOUSANDS OF DOLLARS)

brackets; but not much other change in the general shape of the arrangement.

Use of the extensive shifting assumption without adjustment produces a noticeable change from the reference case. The top bracket's rate is lower and in the large the structure is roughly proportional between incomes of $2,000 to $9,999. The adjustment with the extensive shifting assumption mainly shows up as a rate decrease for the four highest income brackets.

VI. CONCLUDING REMARKS

Based on our calculations for the four major component taxes, it appears that the General Excise Tax and the Property Tax are the ones which show congruence with the total tax rate structure. We can reasonably conclude, then, that the total tax structure estimates come out as they do primarily because of the excise and property tax rate structures, as modified by the rate structures of the personal income and fuel taxes. The question of what accounts for the shape of the estimates of these components, has also been discussed.[28]

It is important that our calculated rate patterns be viewed as estimates, sets of estimates at that. To the extent that our estimates are accurate, one may wish to confront them with his own notion of an ideal or equitable rate pattern. Lack of congruence between the "actual" and the ideal may then indicate a guide for policy changes.

28 This discussion has been rather brief. A more complete account including rather detailed tables is available on request.

APPENDIX

The Data: Its Use and Some Bias

1. Hawaii state income tax return data[1] was chosen because it provides size bracket distributions for various income source components which were required for the allocation of taxes to brackets by income sources. Use of this tax return data implies that the unit of account, or individual member of the group which makes up the bracket, is the Hawaii state personal income tax return. Usually this tax return represents more than one individual, and there would seem to be a rough correspondence between the tax return and the family or expenditure unit. Although the inter-bracket uniformity of the distribution of this characteristic of correspondence is certainly doubtful, our figures indicate that the income bracket percentages for both income source and use do not show much variation when based on personal income compared to A.G.I.

2. The very act of aggregation relinquishes the opportunity for distinction among the positions of the members of the group. Therefore these estimates are not useful for a discussion regarding the equal treatment of equals (horizontal equity); rather the concern here is with the treatment of unequals (vertical equity). Of course the wider the income range covered by the bracket, the more costly (in terms of lost detail) is the aggregation practice.

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1 The A.G.I. concept is used both (a) as the criterion for establishing income classes for the purpose of tax allocation and (b) as an index for calculating a set of effective tax rate distributions. Because of this pair of uses, particularly the latter one, it is difficult to avoid association with the implicit assumption that this income concept is the "appropriate" tax base. This assumption is explicitly denied.

In the census data the unit of account is separated into families and unrelated individuals (which may be combined under the general term "household"), whereas the tax return data refer to the aggregated tax returns, which include individual returns and joint returns. Incidentally, the B.L.S. expenditure pattern data uses the family unit, but defines the terms as broadly as the "household" just referred to. Furthermore, the tax return data brackets refer to adjusted gross income (A.G.I.), but the census refers to a money income concept which is different mainly in that transfer payments (such as unemployment insurance, welfare payments, social security, etc.) are included but receipts from the sale of property not part of business inventory (and therefore capital gains) are exluded. Also, the most recent census (1960) reports income for 1959, tax return data for 1960 are available (in fact tax return data are reported annually).

Even though the census unit (family or "household") seems preferable to the tax return, there are other considerations which led to the decision to use the tax return income data. The tax return data include income size bracket distributions by source of income (e.g., wages, profits, etc.) which are necessary for this study. Also, the census data report the number of units per bracket, but not total dollars received (these must be estimated for each bracket by assuming a mean income) whereas the tax returns report dollar totals. Given the selection of the tax return data, there are three related matters to consider in this connection. One is the choice between federal and state income tax return data. The second is the use of tax return income data in combination with the B.L.S. expenditure pattern data which uses a "household" unit and a different income concept. The third is the consideration of some bias involved in the use of tax return data. The second item is perhaps most important and therefore will be covered first.

3. No attempt was made to adjust for the fact that the income data brackets refer to tax returns while the expenditure data brackets refer to "household".[2] Furthermore, it was decided not to adjust for the fact that the expenditure data brackets refer to money income (but including food and housing received as income) after taxes (all income, poll and personal property taxes). In order to make the adjustment it would have been necessary to use information about intra-bracket distributions which was not available. However, the following remarks may aid in understanding the problem.

Some of the units at the upper end of the bottom bracket of aftertax-income would appear in the next higher bracket of before-tax-income, therefore some members of the group would leave but none would enter. From this it follows that there would be entry to and exit from all other brackets except the top one where of course there would be no exit. To the extent that tax payments are absolutely larger the higher the income bracket,[3] the likelihood of a member shifting to a higher bracket (i.e., pre-tax compared to post-tax) is greater the higher is his initial (after-tax) bracket, for any given intra-bracket percentile position. For this reason the number of members shifting out of all brackets (except the top bracket) is likely to be larger than the number shifting in. However, this tendency toward an increasing upward bias (in number of members) is countered to the extent that lower brackets have absolutely larger membership than higher brackets (and as was mentioned the intra-bracket distribution differences are also relevant). Thus this before-tax, after-tax aspect results in some uncorrected overallocation of members to the bottom bracket and underallocation to the top bracket, with balancing type tendencies operating with respect to the other brackets. On the other hand, the B.L.S. brackets count transfer payments as income, but this item is not included in A.G.I. With respect to this aspect of the income concept difference the effect on the bottom bracket is just the opposite as discussed above (consider, for example, that transfers may be viewed as negative taxes), and therefore this pair of forces tend to balance. The same is suggested for the intermediate brackets (where the individual forces tend to balance also).[4] For the top bracket the situation is one of outflow only, which tends to balance the inflow result noted above. Therefore, it was decided that the adjustment was not worthwhile.

So much for the difference in the income concept in these two sets of data. A further point involves the difference in their income brackets intervals. This matter is discussed below in item 5.

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2 See P. Newman (An Empirical Study of the Distribution of the Tax Burden in the United States, 1955-1959, University of Michigan, Ann Arbor, Sept., 1961 (mimeograph to be published), page 4-4 who notes the complexity of the adjustment as explained in Income Distribution in the U.S. By Size 1944-1950, A Supplement to the Survey of Current Business, U.S. Government Printing Office, 1953. Part I, Section 4.

3 This is especially likely to be true because of progressive income taxes.

4. However, note that whereas with the tax aspect there is a force which tends to increase the tendency for outshift bias at higher brackets, with the transfer aspect the tendency toward an inshift bias perhaps decreases at higher brackets (the ratio of transfers/income declines with bracket size, but it is the absolute dollar amount which counts).

4. Let us take a brief look at some bias involved in the use of tax return data. In particular we are concerned with the under $2,000 income bracket. Consider, for example, the excise tax component. The estimated excise tax rate for this bracket is the ratio of tax to income, where tax is the total dollars of excise tax assigned to the bracket, and income is the total dollars of income assigned to the bracket.

Using tax data, the income figure is A.G.I., and the assignment to the under $2,000 bracket is the total from returns with A.G.I. under $2,000. Some of the returns in the category represent income for less than a full year (e.g., a taxpayer who remained in Hawaii for three months during the year and had $1,800 income during that period). Ideally the under $2,000 bracket would represent units with annual income under $2,000. To the extent that fractional year returns appear in this bracket, there is an overassignment of income here (and an underassignment to other brackets).[5] Furthermore we may consider that an overassignment of income to this bracket results from dependents (such as children who work part-time) who file separate returns. An upward bias in the amount of income assigned to the bracket results in a downward distortion of the tax rate estimate.

Now as regards the tax figure (the numerator in the tax/income ratio) we note the following. Tax is assigned to brackets on the basis of either the use or the source income. With respect to the use income, assignments are based upon expenditure parameters (an expenditure parameter for an income bracket is the proportion of total expenditure which is accounted for by the bracket).[6] The B.L.S. Expenditure Survey provides, for particular items, an average expenditure on the item by a member of the bracket. The Survey includes both families and unrelated individuals and classification as to income bracket is based upon the respondent's annual income. To calculate total expenditure on the item by the members of the bracket, the average expenditure figure was multiplied by the number of units (families and unrelated in-

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5 A reasonable judgement is that part of the fractional year returns would be filed by those defined as non residents under the personal income tax law. Our calculations, however, did not include non resident returns, so this source of bias was eliminated. However, it is interesting to note the close comparison of resident and non resident returns in the under $2,000 bracket.

	resident	*non resident*
tax/A.G.I.[a]	1.2%[b]	0.85%[c]
tax/taxable income[a]	3.4%[d]	3.1%[d]

[a] Hawaii personal income tax
[b] $510 thousand/$40 million
[c] $17 thousand/$2 million
[d] $510 thousand/$14.8 million
[e] $17 thousand/$553 thousand

To the extent that non resident returns involve a disproportionately higher number of fractional year returns, one would expect the tax/income ratios calculated above to be higher for the non resident than for the resident returns.

6 In general, the method for calculating the expenditure pattern parameters involves the following steps:

N_i = number of spending units in income (census) bracket i.

E_{ij} = dollars of expenditure by spending unit in bracket i on item j.

$S_{ij} = (N_i)(E_{ij})$ = total dollars of expenditure by spending unit in bracket i on item j.

dividuals) in the bracket. The number of units came from U.S. Census data, where again, respondents were classified on the basis of annual income. Thus the use of income assignment did not involve the aforementioned tax return data bias. The source of income assignment (of the excise tax, for example) would include such bias, because source of income information comes from tax return data (in fact source data is a major reason for using tax return data). However, the upward bias in the tax figure would tend to be balanced by the upward bias in the income figure, and as a result the distortion of the estimated tax rate would be reduced. Therefore, the rates estimated with the conservative shifting assumption, which refer to tax assignments based relatively more on the source of income, would involve relatively less distortion than the extensive assumption rates (which rely more on the use of income assignments). For the under $2,000 bracket the former rate estimates are lower than the latter, and the latter rate estimates involve more of a downward bias.

5. Patterns has A.G.I. brackets $6,000–$7,999 and $8,000–$9,999. In the interest of presenting as much detail as feasible, these two brackets were disaggregated into four brackets: $6,000–$6,999, $7,000–$7,999, $8,000–$8,999, and $9,000–$9,999. This was done by making use of the data on A.G.I. (both total and by source) for these more detailed brackets which appear in Statistics of Income. In Statistics, data for income by source (such as wages, profits, etc.) are given for the U.S. as a whole, but not for individual states. However, the U.S. source distribution data for these more detailed brackets are useful here, especially because of the close agreement of the U.S. source distribution information with the Hawaii data shown in Patterns.[7] In general, linear interpolation is used for the disaggregation.

The B.L.S. Expenditure Survey Study has the following brackets: under $2,000, $2,000–$2,999, $3,000–$3,999, $4,000–$4,999, $5,000–$5,999, $6,000–$7,499, $7,500–$9,999, $10,000–$14,999. and $15,000 and over. The following procedure was used to disaggre-

---

$$\sum_{i=1}^{n}(S_{ij}) = \sum_{i=1}^{n}\left[(N_i)(E_{ij})\right] =$$ overall total dollars of expenditure by all units in all brackets on item j.

$$R_{ij} = \frac{S_{ij}}{\sum_{i=1}^{n}(S_{ij})} = \frac{(N_i)(E_{ij})}{\sum_{i=1}^{n}\left[(N_i)(E_{ij})\right]} =$$ proportion of overall total of dollars of expenditure (by all units in all brackets) on item j assigned to bracket i.

$C_{kj} =$ total dollars of tax k to be assigned by item j, i.e., expenditure on item j is designated as the basis for the assignment of dollars of specified tax k to income brackets.

$$T_{ijk} = (R_{ij})(C_{jk}) = \frac{C_{jk}S_{ij}}{\sum_{i=1}^{n}(S_{ij})} = \frac{C_{jk}(N_i i)(E_{ij})}{\sum_{i=1}^{n}\left[(N_i i)(E_{ij})\right]} =$$ the dollars of this specified tax k assigned to income bracket i on the basis of expenditure on item j.

7 The calculations were made, but will not be included here.

gate the pair of brackets between $6,000 and $9,999 into four brackets at $1,000 intervals. Census data shows the number of units (families and unrelated individuals) for each of the brackets to be constructed. The $7,000–$7,999 bracket was constructed by assigning the $6,000–$7,499 expenditure pattern to ½ of the units in the $7,000–$7,999 range and assigning the $7,500–$9,999 expenditure pattern to the other ½ of the units in the $7,000–$7,999 bracket. The $7,500–$9,999 expenditure pattern was assigned to both the $8,000–$8,999 bracket and the $9,000–$9,999 bracket The $6,000–$7,499 expenditure pattern was assigned to the $6,000–$6,999 bracket.

It is evident that this procedure involves bias. The expenditures of the $6,000–$6,999 bracket are certainly biased upwards and the same probably is true for the $8,000–$8,999 bracket. In the $7,000–$7,999 bracket the use of the $6,000–$7,499 and the $7,500 and $9,999 expenditure patterns introduce a downward bias and an upward bias respectively, and it is not clear which way the balance goes. The expenditures of the $9,000–$9,000 bracket are certainly biased downwards. It follows that the calculated tax assignments based on expenditure patterns and the resultant tax rates are biased in the same directions as the expenditure estimates.

The available data was insufficient to support further adjustments. But although the results (tax rate patterns) are distorted by the bias, the distortion is not serious for the degree of precision claimed for a study of this type.

To estimate the magnitude of the distortion, consider the $9,000–$9,999 income bracket as a case in point. It can be shown that where R_i = the proportion of expenditures accounted for by bracket i,

$$R_i = \frac{R_i\,(1+\alpha)}{1+\alpha R_i},$$

where α = the percentage adjustment for bias in the average expenditure by a member of the i-th bracket.

In the $9,000–$9,999 bracket, R = .054, for all goods and services. If we suppose that the α = 10% is the correct upward adjustment, R' = .0587. With α = 20% in this case, R' = .064. Thus even if we judge the bias (in the average expenditure by a member of the bracket) to be as great as 20%, the resulting distortion in the tax rate estimate for the bracket is less than 20%, which in this case is less than 1 percentage point.[8] In fact, a bias of α = 10% seems more reasonable,[9] and here the resulting rate distortion is about ½ of 1 percentage point.[10]

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8 Let T = tax, Y = income, and t = T/Y = tax rate, all for a particular income bracket. Also, let s = the bracket's share of total tax = X, so T = sX. Thus t = sX/Y. Now let t' = s'X/Y, where s' = $s(1+\gamma)$, The t' = $s(1+\gamma)S/Y = t(1+\gamma)$. Therefore the percentage change in t = (t'−t)/t = γ, and γ = (R'−R)/R.

9 The reasoning behind the judgement that 10% is more reasonable is as follows. Suppose the average expenditure for the $7,500–$9,999 bracket equals that of the $8,750 member, and the average expenditure for the $9,000–$9,999 bracket equals that of the $9,500 member. Then we would expect the expenditure difference to be less than $750 (the income difference). The data shows about $6,900 expenditure for the $7,500–$9,999 bracket, 10% of this is $690, and 110% is about $7,600. Now note that the ratio of expenditure to income may be calculated as 6900/8750 = 79% or 6900/8500 = 81%, and 80% of $9,500 is $7,600. So 10% bias seems to be a fairly decent judgement.

10 As was noted in the text, a result of the interpolation of the income and the expenditure pattern data is that the interbracket detail of the tax rate estimates in the middle income range may not be as significant as that of the rest of the income scale.

6. Now a few remarks are in order with regard to the total amount of income to be distributed. For the purposes of this study it is appropriate to consider information from both taxable and nontaxable returns. The data from Patterns shows income (A.G.I.) of about $1,036 million (net of about $11 million nonresident income and $1 million loss group) based on about 193,000 returns (net of about 4,000 nonresident returns). Statistics indicates about $1,148 million based on about 196,000 taxable returns. Estimates from Census data run about $1,179 million using an overall mean income figure, but aggregations of bracket totals estimated by midpoints run between $1,320 and $1,324 million. The amount from Patterns is about 87% of the Statistics figure. It was decided not to make an upward adjustment in the Patterns data because of lack of information necessary to make anything other than a uniform adjustment (e.g., divide each bracket income total by .87), which would not be very enlightening given the emphasis of this study on the relative situations of brackets.

DRAFT RESOLUTION*

The use of changes in the tax system as a part of a stabilization policy is supported by both experience and theoretical analysis. Changes may be made to assist in the stabilization of economic activity, the price level or the balance of payments. Actions useful for one of these three objectives may be neutral or even adverse from the standpoint of others, although there is no general agreement on their effectiveness. Taxation should be considered in the context of all other instruments of economic policy.

Though some tax changes to assist stabilization may be useful, there are many technical, legal and political difficulties in securing wise and timely action. Furthermore, tax changes useful for stabilization purposes may be regarded as inequitable or inconsistent with tax policies designed to encourage long-term economic growth or long-term international capital movements. Such disadvantages are intensified if changes are made too frequently.

When taxes are used for stabilization purposes one must try to prevent lasting distortions in the competition between companies within an industry or serious changes in the general economic conditions for an industry.

Since the end of the Second World War strong efforts have been made to reach general international agreements to avoid the use of taxes as an instrument of trade policy. Up to now significant results have been achieved with respect to the international exchange of goods and services. Corresponding international agreements are lacking regarding international movements of capital. A general opinion has been expressed at this congress that international legal rules in this field would be helpful in order to avoid distortions. Stabilizing policies or shortterm national interests must not obstruct the development of such agreements.

Where several states cooperate in free trade areas or common markets these problems of a national and international character will assume greater importance.

Long-range planning in individual enterprises has been of growing importance for industrial and economic growth since the Second World War. Furthermore technical development often had made investment more time-consuming. Measures of stabilization policy in the short run must be developed in the light of both national planning and planning in industry. To make such coordination possible, close cooperation between government and industry is required. Experience has shown that the effectiveness of tax measures required for stabilization purposes will increase if the tax measures are coordinated with the permanent tax system. Also legal considerations of a general nature require such a coordination in order to assure legal certainty and to facilitate the application of tax rules by the tax authorities and the taxpayers.

Changes must be introduced with great care in order to minimize unintended effects on taxpayers. The Congress regrets that deviations from these legal principles have occurred after the Second World War.

The Congress has paid great attention to the use of changes in the corporate taxes as a part of stabilization policy. Changes in tax rates and depreciation rules as well as the use of investment funds and credits require, from the point of view of business economics, intensified research.

TVA (the value-added tax) has been introduced in France, Denmark and Germany in order to achieve a uniform taxation of consumption with minimal distortions in industry and trade. It might well be that the TVA could be used as a measure in stabilization policy. However, experience of such use is lacking. Such an application would most probably be complicated from an administrative point of view.

In the discussion which has included several other taxes as e.g. taxes on individual income, compulsory savings and tax incentives to stimulate voluntary savings, the need for highly skilled research regarding the role of taxation in stabilization policy with reference to the legal and business economy aspects has been stressed. The nature and the scope of the subjects requires a considerable scientific cooperation between political economists, tax lawyers and business economists.

*) First subject: Changes in the tax system as a part of stabilization policy – their technical and legal implications.

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Convention between the Government of the United States of America and the Government of the United States of Brazil for the Avoidance of Double Taxation with respect to Taxes on Income

T.V.A. PARADOX

One of the most important paradoxes of the introduction of the T.V.A. in E.E.C. as a "neutral" tax is that the neutral T.V.A. may be used as an egoistical nationalistic competitive device by one member state against another or by the E.E.C. against third party countries. This paradox is explained by Mr. Eggert Møller in his article on T.V.A. and the Renaissance of tax neutrality in this Bulletin issue. Irrespective of whether countries like the T.V.A. or not, they will have to introduce it because international competition compels them to. In addition having once introduced it, they are compelled to attempt to be the first to increase its burden relative to those of other taxes, for the same reason (see p. 448 of this issue).

The battle against international trade competition using tax measures as a weapon is therefore still going on, in spite of "neutral" T.V.A. The new weapon may even be more dangerous than the old one of "playing tricks' at the frontier with the turnover taxation at imports and tax refunds for exports. The latter resulted in the E.E.C. draft directive published on p. 461 et seq.

The battle against international trade competition using tax measures is also one of the subjects of the South African budget 1967/68, reported by Dr. Spiro on p. 451 et seq. The south African Minister of Finance appealed to exporters to spare no effort to capture overseas markets and entended export allowances.

The same concept is present in the article on recent tax modifications in Argentina. The Government is tending to use tax measures to help increase Argentine exports. It may be interesting to note that the Argentine Government has carried out a detailed study of the feasibility of replacement of the sales tax by a tax on value added. This kind of study seems to be becoming an international fad nowadays. E.g., a committee appointed by the Rhodesian Minister of Finance to examine the advantages and disadvantages of introducing a T.V.A. in Rhodesia has just completed its report.

We are anxious to know what the "value-added" will be to international welfare by the introduction of the "value-added tax".

DR. J.C.L. HUISKAMP

* * * * ARTICLES * * * *

MOGENS EGGERT MØLLER*):

ON THE VALUE-ADDED TAX IN DENMARK AND THE EUROPEAN ECONOMIC COMMUNITY AND THE RENAISSANCE OF TAX NEUTRALITY

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1. RENEWED IMPORTANCE OF TAX NEUTRALITY

1.1. The discussion concerning the proposed objectives of the European market groupings, and the steps to be taken in order to attain these objectives, has revived interest in the old problem of tax neutrality. One of the recognized ways of attaining the proposed objectives – and, as far as EFTA is concerned, the most important one of all – is the removal of customs barriers between member states. The removal of these barriers may per se be considered a decisive step towards tax neutrality when seen in relation to the trade between member states.

1.2. In so far as tariff reductions remove the protection of trade and industry in the individual countries, the question arises whether

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the existing internal taxation rules are suited to the new situation which arises when goods start flowing in the larger market area. To this must be added the adaptation difficulties resulting from the greater facilities for making capital transfers and the greater mobility of manpower concurrently introduced by the EEC.

1.3. The EEC has anticipated the new motive which member states will have for changing their internal legislation, including their fiscal legislation in the widest sense of the term, with a view to increasing protection. The effect of all this is that the market groupings consider it important that the legislation of member states "will not distort the competitive conditions" existing between them. Possibly, there are many who find the demand for neutrality in competition equally well and directly motivated in the desire to obtain the greatest possible freedom of action in the economic development of the market grouping, but the Treaty of Rome itself naturally does not support either liberalism or socialism. It is in that respect "politically neutral".

Concerning 1.2. The EEC has mainly devoted its attention to the idea of a so-called harmonization of the legislation of member states in respect to indirect taxation, presumably under the impression that the financial dispositions of the population are primarily affected by indirect taxation. It is no mere coincidence, for instance, that there are no municipal excise duties—at least in Denmark. Any differences in such local duties would engender shopping traffic across the municipal boundaries and affect settlement and the location of industrial and commercial firms to such a degree that the fiscal advantages would be almost insignificant. The greater the integration of member states in the market grouping, the greater this tendency would be.

Concerning 1.3. To this must be added that indirect taxes are particularly well suited—and therefore tempting—to use as a substitute for customs barriers.

The preliminary results of the EEC's efforts at harmonization is the Council of Ministers' Resolution of 11th April 1967 concerning the introduction of a common tax on value added (TVA), which the taxation theorists of the EEC have, in fact motivated by "neutrality"[1]). At the introduction of the Bill for the Value-Added Tax in Denmark, which Bill has now been passed, the neutrality of this tax was repeatedly mentioned in support of it[2]).

But What is the true Meaning of Neutrality?

2. KNOWN VARIANTS OF THE PRINCIPLES OF NEUTRALITY

Formulations of the principle of tax neutrality vary widely. Common to them all, however, is the fact that they establish as a fiscal objective (either an objective per se or a means of attaining other objectives) that taxes should not be allowed to have repercussions on certain social conditions.

Reservation

It seems necessary at this stage to point out that this paper is written by a jurist and that it therefore contains no expert economic analyses. This part of the work will have to be undertaken by others.

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1) See "Amtsblatt Der Europäischen Gemeinschaften" of 14th April 1967 (G 1203 B) p. 1301ff.

2) See "Redegørelse vedrørende Mervædiagift" (Report on the Value-Added Tax) prepared by the Department of Customs and Excise, Copenhagen, 1964 (in the following called "the Danish Report"), e.g. on p. 5 ff., and "Forslag til Lov om almindelig omsætningsafgift" (Bill for a General Sales Tax) introduced on the 7th December 1966, p. 12, left column, paragraph 4: "When preparing the Bill stress has been laid on drafting the provisions so as to maximize the neutrality of the tax".

2.1. Vertical Neutrality or Neutrality of Distribution

In a short survey in "Taxation and the American Economy"[3]), W.H. Anderson expresses the opinion that there have appeared at least three different concepts of neutrality. The first of these concepts is described as follows: "The leave them as you find them principle argues that a tax should not change the rank in which a person stands in the hierarchy of wealth and income. The principle is justified on the basis that human satisfactions and economic incentives will be less affected if people are permitted to retain the same relative economic rank after taxation as they had before."

2.1.1. In so far as a redistribution of income and wealth is intended, e.g. by means of a progressive taxation of income and inheritances, the above principle must be said to have become obsolete[4]).

2.1.2. A modern variant might be that a taxation reform would have to take into account, i.e. be neutral as regards, the existing "social balance". Such a relative neutrality of distribution has been maintained in connection with the introduction of the Danish value-added tax, steps having been taken to counteract its regressive effect by adjusting income tax rates; by introducing personal grants, which are inversely progressive in relation to income; by increasing the existing child grants; and by introducing subsidies granted to reduce the prices of certain dairy products. In this way we have obtained a system of direct and indirect negative taxes the avowed political objective of which is relative neutrality of distribution.

2.2. The Principle of Neutrality in the Allocation of Resources ("Neutrality in the Allocation of Resources")

Anderson goes on to say:

"A second definition of neutrality is taxation that does not alter the allocation of resources. This concept of neutrality is justified because it results in benefical effects upon the morale of taxpayers, in the optimum allocation of resources, and in the maximum satisfaction of consumers."

This principle of neutrality in the allocation of resources plays an important part in the EEC as appears, inter alia, from the Common Market model of tax on value added adopted by the Council of Ministers on the 11th April 1967, which is to become operative in all six countries by the 1st January 1970 at the latest, and which came into effect—so to speak verbatim—in Denmark on 3rd July 1967. The ideologists in Brussels have developed a fairly effective philosophy or doctrine. Reugebrink[5]) writes, e.g.:

"Seen from a point of view of political economy, the primary objective of all fiscal regulations really is to attain to maximum welfare in the economic community ("Volkswirtschaft"); in other words: an optimum application of available productive resources. This objective is called the welfare principle. According to this basic principle taxation should disturb price conditions as little as possible—apart from cases where it is necessary to take legislative action for political or other reasons. The usual function of the price mechanism is to control the allocation of finished products and factors of production

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3) Prentice Hall, New York, 1952, p. 54.

4) The principle has been discussed for centuries; see "Steuerpolitische Ideale", by Fritz Karl Mann, Jena 1937, i.a. p. 247.

5) See J. Reugebrink: "Enkele Beschouwingen over de Neutraliteit van de Omzetbelasting", Deventer 1965, p. 14. – German translation in E.W.G., Kommission, Generaldirektion für Wettbewerb, Direktion für Steurfragen IV C 2, 4779/IV/66-D; see p. 8. Only the German translation will be used here and in the following.

by means of a large number of expenditure commitments ("eine Vielzahl von Verwendungen"). Assisted by the price conditions ruling on the market, and with their limited incomes, consumers will endeavour to procure those very goods which give the maximum satisfaction. If these price conditions are disturbed by taxes, the result will be distortion of the optimum allocation of productive resources to the detriment of the welfare principle."

Whereas it may be somewhat difficult to determine how direct taxation affects the allocation of resources, there seems to be no doubt that, in this very respect, TVA is the most neutral of all indirect taxes; see 5.3.4.2.

2.3. The Neutrality of Motive

Anderson concludes his survey as follows: "Neutral taxation has recently been defined also as that taxation which makes the tax burden independent of choices made or actions taken by the taxpayers. The justification of such a concept of neutrality is the prevention of widespread avoidance and undesirable economic repercussions which would otherwise limit the degree of progression in the tax system."

According to tradition the neutrality of motive acquires its chief importance in relation to direct taxes (choice of the time and mode of realization of income etc. — in short the opposite of "taxplanning"), while neutrality in the allocation of resources in particular is considered to acquire importance in relation to indirect taxes.

However, there may be presumed to be some overlapping of these two forms of neutrality as far as indirect taxes are concerned. For value-added taxation is intended not to affect the choice of consumer goods, the structure of the business community etc. It can only be a question of "a certain amount of" overlapping, however, since the chief exponents of TVA are presumably mostly macroeconomists who would occasionally seem, from a jurist's point of view, to be dealing rather rigidly with abstracts when presuming motives in "the economic man". On the other hand, it will often appear to jurists (at any rate to the present author) that microeconomists are more realistic in their psychologizing motivation analysis. In further illustration of this point see below 5.3.2.2.

2.4. Neutrality of Costs

2.4.1. In her book "The Tax on Value Added"[6]), Clara S. Sullivan deals at some length with the American conception of TVA regarded as a cost similar to other business costs. On page 41, for instance, she mentions: "... the analogy between the value-added tax and the cost of business purchases of factors of production...".

Sullivan makes no mention of neutrality in this connection, but it is probably quite possible to do so.

In my opinion it is possible to visualize a neutrality of costs in the sense that firms should defray the costs with which they burden the community. It is of course open to discussion how such costs should be computed. Account may thus be taken of the direct public expenses incurred by the existence of a firm (the Danish "dækningsafgift", which is a special municipal tax imposed on industrial real property for services rendered, is motivated by the necessity of covering these expenses[7]),

6) Columbia University Press, New York and London, 1965.

7) See "Forslag til lov om ændring af lov om beskatning til kommunerne af faste ejendomme. (Om dækningsafgift)" (Bill for the Amendment of Act on Municipal Taxation of Real Property), introduced on 22nd February 1967, "Explanatory Notes on the Bill", Paragraph 2: " — that as a special tax of 5 per mille does not provide adequate cover for the expenses incurred in the construction of roads, streets, parking grounds, sewers, and the maintenance of fire-fighting services, civil defence etc., with which such properties burden the municipalities, it is proposed that the maximum rate be raised to 10 per mille."

or account may be taken of costs in a wider sense. However, it is more important to establish a basis of tax assessment in the case of each individual firm so that the reciprocal tax burdens of firms correspond to the different reciprocal expenses of the community incurred by the existence of the firms.

The neutrality of costs will increase the above-mentioned neutrality in the allocation of resources by including payments to and from the public sector in the analysis, but it will obviously be difficult to carry it through in practice.

2.4.2. There is also the possibility of concentrating on external relations with a view to investigating whether neutrality exists between the countries as regards the amount of taxes paid by firms. Such investigations are being conducted in the EEC, which is in fact attempting to harmonize the effects of direct taxation, see below: 5.3.2.2. which deals with the effects of costs.

2.5. Impartiality, Neutrality as Regards Pressure Groups or Sectional Interests

In "Neutrality in Taxation"[8]) H.M. Groves advocates neutrality in the allocation of resources in a general sense, but he adds: "...: not that legislators can never improve upon the natural order in this respect (optimum allocation of resources and the maximum satisfaction of consumers), but such improvement will not be attained by deliberate favoritism or bungling."

Groves emphasizes in his paper that impartiality is an independent neutrality principle, a kind of anti-lobby variant which naturally arouses interest also outside the U.S.A.

Shipping is probably a case in point. The shipyards were exempted from paying Danish TVA at the last moment. Nevertheless, they "naturally" retain their full right to get refunds for paid TVA. The tightening of the rules of depreciation for the purpose of counteracting the effects of the so-called "balance-sheet purchases" (i.e. last-minute purchases effected in order to reduce the taxable income by utilizing the special facilities offered for depreciation of assets; in short abuse of incentive taxation), see 5.3.2.2., will not affect ships, which are in all other respects treated in the same way as machinery and equipment, for which the depreciation allowance in the first year will be reduced from 30 to 15 per cent.

The mobility of ships is one of the reasons why they are especially benefited by international competition in the form of "deliberate favoritism".

2.6. Horizontal Neutrality

Groves also expresses an interesting and suggestive opinion concerning the relationship between the neutrality principle and something resembling the ability-to-pay principle, ("equity and justice, which include an interest in economic equality as well as in impartiality"): "Neutrality has to do less with the standards applied to the over-all distribution of the tax load and more with the even application of those standards once they are chosen. There is no inference of conflict between the two canons. ... taxes should be equitable and they should deviate from neutrality only for an adequate public purpose."

The interventionism of our century has of course asserted itself strongly in the field of taxation. This helps to explain why the neutrality principle has been thrust into the background for many years. Nevertheless, it is probably a generally accepted idea that neutrality "ought to" prevail where it does not run counter to the public interest. Danish instances of current interest are: owners (of single-family houses) as opposed to tenants,

8) See "National Tax Journal", March 1948, p. 18 ff.

and wage and salary earners as opposed to independent traders. Overlapping with 2.5. may therefore occur in extreme cases.

Summarily to reduce neutrality to the "proper" elaboration of the means once the standard has been set is presumably a too easy solution.

If neutrality really is conducive to a better allocation of resources, and therefore presumably to economic growth, e.g. in the EEC (and that is the general opinion), we are faced with the classic problem: Are we to concentrate on dividing the cake into more equitable pieces or on making them all bigger; the results of our deliberations will then not always be foregone conclusions. The neutrality principle is just as important to TVA as the ability-to-pay principle is to income tax. In this sense the two principles may be said to be placed on an equal footing.

It can hardly be doubted that Groves' definition is well in keeping with the situation in the United States at the time when he wrote his paper (1948).

2.7. Groves has touched on the legal neutrality principle by emphasizing the impartiality concept.

Reugebrink writes on page 2: "Consequently, I shall first deal with the question whether a maximum realisation of the legal nature of sales tax implies that such a tax must remain neutral in relation to specific conditions". And later on, at the bottom of page 3: "Since a general sales tax is levelled at private expenditure it appears obvious to me that there must be some relation between the amount of taxes or duties imposed and the volume of expenditure. However, the smallest justifiable demand that can be made on a tax or duty probably is that the tax burden of the individual taxpayer can be measured, so that whatever is equal can be treated equally and whatever is unequal can be treated unequally."

He goes on to "prove" that value-added tax is superior to cumulative sales tax as it is based on a kind of legal neutrality.

Perhaps Reugebrink can be said to border on "conceptualistic jurisprudence", but my main point is that his exposition also contains one of the central ideas of the TVA ideology, which is based on that very same concept of equity, and which is interspersed with a number of quite daring logical conclusions; for an instance of this see: 5.3.1.2.3.2.

Reugebrink's postuláte concerning legal neutrality may be "translated" as follows: "The cumulative sales tax produces an incalculable and unpredictable incidence (shifting of the tax burden). TVA produces a clearer incidence that may be more easily calculated. Consequently, I prefer TVA." His real problem resembles, and may possibly overlap, the problem posed in 2.: "even application". My temporary conclusion is that a "purely legal" neutrality principle cannot be formulated without reference being had to economic phenomena and problems, perhaps with the exception of the problem concerning a possible infringement of the constitutional equality of rights by the overtaxing of religious or racial minorities.

Reugebrink is moreover of the opinion that the tax on value added clashes or conflicts with the ability-to-pay principle in that the tax is regressive. Or expressed a little more cautiously:

In its consequences (regression) the tax on value added offends against the general conceptions of the ability-to-pay principle (e.g. progression).

2.8. External Neutrality

Reugebrink further points out the fundamental cause of the success of value-added tax in Europe, viz. that it is considered to be externally neutral, i.e. neutral in relation to foreign trade, that is if the destination principle is applied. The origin principle will, on

the other hand, indicate the producer-country principle of taxation (and not the consumer-country principle of taxation) as determining neutrality. External neutrality applies chiefly to the EEC (the inter-European allocation of resources), but the principle is also applied in organizations like GATT and EFTA.

2.9. Neutrality in Competition

Finally, Reugebrink mentions the typical EEC term "wettbewerbsneutral". This and similar terms pervade many articles of the Treaty of Rome (e.g. Articles 92 and 95-102). The desire for neutrality in competition evokes a kaleidoscopic wealth of associations in EEC officials, these associations having probably only the dynamic EEC pragmatism in common. It is therefore able to overlap almost all the variants mentioned above and in the following.

Whereas TVA is systematic and fixed, "distortions of competition" (Wettbewerbsverzerrungen) are combatted in the field of excise duties and direct taxes wherever the distortions are considered to be worst at any given time, and, as already intimated, this is done without any further thought to a delimitation and precise formulation of the principle of neutrality in competition. The problems relating to neutrality are therefore not restricted to taxes which affect the prices of goods directly through a shifting of the tax burden ("waren- oder preisbezogen"), the so-called indirect taxes; they also include taxes affecting the prices of goods and the competitive capacity indirectly ("gewinnbezogen" etc.), the so-called direct taxes.

2.10. Purely Fiscal

Fritz Neumark criticizes the neutrality concept in his book "Wirtschafts- und Finanzprobleme des Interventionsstaates"[9]). In my opinion his criticism seems to overshoot the mark and to be lacking in some of the finer shades.

On page 393 he writes: "At present the utopian and chimeric character of tax neutrality has been generally realized, and the earlier liberalistic opinions concerning fiscal equality are being criticized for their narrowness and formalism". And on page 131: "... Tax neutrality (is considered an unapplicable principle because) ... its content is extremely vague (verschwommen). ... In this respect the "purely fiscal tax" is better, ... It is unambiguous, in the sense that taxes are levied in order to provide revenue for the state."

The purely fiscal tax may therefore be characterized as a blindly neutral tax. There is at least no attempt at intervention or "nicht-fiskalisch motivierter Steuermassnahmen" (page 132). Nowadays it is more likely that an occasional attempt will be made to create what may be termed a "blind" contractive effect of fiscal policy, e.g. an effect that will "limit consumption", on the assumption, of course, that it is at all possible for "blindness" to exist in our enlightened age.

This blind neutrality has perhaps been prevalent in many situations, especially earlier, and not least in respect of excise duties. The "blindness' referred to applies only to taxes per se, a ceteris paribus clause being inserted in respect of the application of the revenue from taxation For further details see: 5.3.1.2.1.

3. RENAISSANCE OF THE CANONS OF NEUTRALITY

3.1. Previous History

3.1.1. Main Events in the Historical Development of Value-Added Tax.

In 1919 Wilhelm von Siemens wrote about "Veredelte Umsatzsteuer" ("Purged Turnover Tax"). He was a business man and governmental consultant and suggested the

9) I.C.B. Mohr, Tübingen, 1961.

so-called subtraction procedure (deduction of the increase in value during preceding stages of production and turnover) as a means of abolishing the double taxation resulting from the German cumulative turnover tax. Already two years earlier, Thomas S. Adams had first expressed his views on "The Taxation of Business" in the "Proceedings of the Eleventh Annual Conference on Taxation of the National Tax Association". Adams, a professor at Yale University and government consultant, did not recommend the subtraction procedure. Instead he suggested that the credit procedure (a credit or refund for taxes paid) be introduced in its place. His tax: Taxation on Value Added (TVA), is largerly based on a "cost principle". Adams' value-added tax is called "the income type of sales tax". He rejected depreciation allowances, the result being "the gross product concept". Depreciation pro rata temporis ("net income type") was recommended at a later stage. "The Michigan Business Activities Tax", which was introduced in 1953, corresponds to TVA net income type, "... a tax paid by a business firm which is measured by its contribution to the value of aggregate product or income originating in the taxing jurisdiction and which is justified as payment for public services to business." (Sullivan, page 300). Adams' tax-credit procedure has been superseded by the "subtraction procedure". Incidentally, American doctrinal history is too long and too complex to be recounted in the present paper.

Professor Carl S. Shoup is today one of the leading tax theorists in the U.S.A. He was appointed head of the so-called Shoup Mission which prepared a Report on Japanese Taxation I and II, 1949 and 1950, in which TVA was recommended as principal tax. The act was passed but never took effect.

Taxe sur la Valeur Ajouté (TVA) was introduced in France in 1954. This tax has been modified and improved innumerable times, most recently in 1966 when the rate was reduced from 25 to 20 per cent, while TVA was extended to comprise the retail trade. It has developed gradually and through many successive stages from a tax on production to a tax on consumption that is getting closer and closer to the EEC model.

On 11th April 1967 the Council of Ministers of the EEC adopted a proposal for the introduction of TVA in all six member states before 1st January 1970.

The Danish tax on value added became effective on 3rd July 1967.

According to "Umsatzsteuergesetz (Mehrwertsteuer)" of 29th May 1967, Sect. 33, TVA is to become effective in Western Germany on 1st January 1968 (see "Bundesgesetzblatt" Teil I, 1967, No. 30, published in Bonn on 2nd June 1967, pp. 545-567).

The Netherlands have prepared a "Studienentwurf", see "Bulletin for International Fiscal Documentation", 1966, pp. 488-507.

The Swedes are deliberating, see S.O.U. 1964: 25 (Nytt Skattesystem) and S.O.U. 1965: 28 (Remissyttranden).

Finland has a kind of TVA that is limited to the retail trade. The cumulative effects (the double taxation) on investment goods are expected to increase export prices (f.o.b. prices) by 3 to 6 per cent.

3.1.2. According to Groves (1948) and H.W. Anderson (1952), Carl S. Shoup is one of the originators of the concept of neutrality in the allocation of resources which played a decisive part in the elaboration of the European tax on value added which is using neutrality in consumption as point of departure.

3.2. The Neumark Paradox and the Break-through

As late as in 1961, Fritz Neumark expressed skepticism concerning tax neutrality in his book "Wirtschafts- und Finanzprobleme des Interventionsstaates". Under the influence of

the crises and wretched social conditions of the twenties and thirties he became a staunch supporter of intervention.

Neumark's book is dedicated to his friend Carl S. Shoup.

The so-called Neumark Report[10]) was published in 1962. It was named after the above-mentioned author who was elected chairman of the committee, the other members of which were a "Staatsrat" from Luxemburg and nine professors, all of whom came from the EEC, except for Shoup who came from New York. The Neumark Report lays the foundation of the philosophy of taxation of the European Common Market, neutrality makes its break-through, and the TVA consumption-type variant is recommended in the same connection.

Below (5.3.2. and 5. and 6.,) an attempt will be made to throw light on the special TVA consumption-type variant by citing examples from the Danish value-added tax, which is patterned on the EEC model as regards justification as well as structure and details. It is true that, at the last moment, the Folketing (the Danish Parliament) did introduce some deviations from the EEC model, but these are relatively few and insignificant. The power of the press was once more emphasized by the fact that newspapers were exempted from the tax while retaining their full right to get refunds for paid TVA.

4. AIMS OF THE INVESTIGATION

The above survey and the below outline should, of course, be regarded only as a preliminary to a more detailed analysis of tax neutrality.

Even an analysis of the approach to the problem may arouse interest by itself since it is presumably fairly doubtful how much can be achieved by using quantitative methods of investigation when experiments are practically out of the question. To this must be added that it is likewise doubtful whether or when such quantitative methods will be used in this field. Such an investigation would take a long time and be very costly. And the country has to be governed and is being governed—so far without any well-founded knowledge of the causal relations in this important field.

What, then, would be the best result that could be obtained from this modest attempt at a legal analysis of the problems of tax neutrality:

1) To establish a method which
a) gives a clearer picture of the political objectives underlying the existing rules, and which
b) raises the question whether the political objectives were in fact attained when regard is had to the drafting and application of the rules.

   This method can and should of course be applied also to rules and parliamentary bills at the preparatory stage.

2) To demand that politicians should understand more clearly the political objectives and the appropriateness of the measures taken than they have so far done.
a) This should result in greater clarity in the political debate,
b) and, as far as the administration and the law courts are concerned, in greater regularity—fewer doubtful interpretations—and therefore in greater predictability, and
c) as far as the citizens are concerned, in a better understanding of the purposes for which rules are laid down.

During the debate politicians might conceivably try deliberately toconfuse ends and means, but confusion will generally be unintentional.

10) E.W.G. Kommission, Bericht des Steuer- und Finanzausschusses, (8070/2/XII/1962/5).

5. AN ANALYTICAL EXPERIMENT

5.1. General:

5.1.1. A purely abstract definition of tax neutrality does not help much. It may easily become vague in the same way as a purely abstract definition of liberalism.

The concept will be more readily understood viewing it in the light of history. Concepts like "Classic Liberalism" and "Neo-Liberalism" evoke certain associations in all economists. One of these associations is tax neutrality.

Tax neutrality can (when considered in this vague and undetermined way) be perceived as a fiscal objective per se, e.g. by liberalists and jurists of the old school.

Typically, however, tax neutrality will be a means—or one out of many means—of achieving, e.g. greater economic growth, integration within the EEC, a larger foreign trade, a more efficient assessment of taxes, prevention of tax avoidance etc. Naturally, no consideration has been given in this connection to the question of whether greater economic growth can best be achieved by adopting a fundamentally interventionistic or a fundamentally neutral fiscal policy.

This description of tax neutrality as a "means" does not prevent concepts of tax neutrality from being just as dominating as, e.g., concepts of the ability to pay tax. The Danish value-added tax is thus dominated by the neutrality principle in the same way as the Danish income tax is dominated by the ability-to-pay principle.

5.1.2. Every time the term "tax neutrality" is met with, the following questions should be asked:

a) To which variant does the term refer?
b) Can the variant be linked up with any specific political objective?
c) Are the techniques explained?

Example: TVA in the EEC variant:

Concerning a) Neutrality in the allocation of resources.
Concerning b) The desire for economic growth and integration.
,, c) The structure and details of the acts.

5.1.3. A systematic comparison of the neutrality principles with the ability-to-pay principles would be useful. The problem is of current interest in Denmark where the new value-added tax, which is greatly prized for its neutrality, has had to be supplemented by rules governing personal grants and subsidies granted to reduce the prices of certain dairy products.

It may be useful to compare the neutrality principles with the benefit principles, traces of which can still be found today in various parts of our tax system, e.g. the tax on motorcars and the rules governing the special municipal tax ("dækningsafgift") imposed on industrial real property for services rendered. It is beyond the scope of a jurist to analyse the neutrality principles on the basis of the method and terminology used in the still widely discussed welfare principles of political economy, but he may of course seek support and guidance from economists.

Altogether, the systematic comparison of the fundamental principles involved here calls for cooperation and a splitting up of the work between jurists and economists.

5.2. Specific:

Neutrality Situations

There is an infinite variety of neutrality situations. Among the most important "economic" situations are:

a) Choice of type of business organization.
b) ,, ,, method of financing and capital investment.
c) ,, ,, time, method and place of initial purchases and realisation.
d) ,, ,, domicile and/or residence.
e) ,, ,, the firm's situation.
f) ,, ,, method of production (capital-intensive as opposed to labour-

intensive—large-scale operations as opposed to small-scale operations etc.).

g) Owner (of single-family house) as opposed to tenant.

h) Choice of form of cohabitation (the problem of joint income tax assessment).

j) ,, ,, consumer goods.

The "non-economic" situations are also well known. There should be no discrimination (and this applies to taxes, too) on account of race, religion, political affiliation, social status etc.

5.3. Some Fundamental Distinctions

It is therefore possible to tackle the problem of neutrality either by presenting—more or less critically—the opinions of others, or by placing the problem in its proper setting in the history of ideas, or by comparing the principle with others, such as the ability-to-pay and the benefit principles, or by attempting to give precise definitions in the analysis of ends and means, or by concentrating on certain neutrality situations, or by combining two or more of the above-mentioned possibilities.

But there are still more possibilities.

My six distinctions are:

1) Intentional versus Unintentional Neutrality.
2) Neutrality in Form versus Neutrality in Substance.
3) Specific Neutrality versus General Neutrality.
4) Neutrality Observed in Relation to the Past versus Neutrality Observed in Relation to the Future.
5) Neutrality of Direct Taxes versus Neutrality of Indirect Taxes.
6) External Neutrality versus Internal Neutrality

5.3.1. Intentional versus Unintentional Neutrality

5.3.1.1. According to traditional usage intervention can presumably only be regarded as intentional. The same must be held to apply to non-intervention.

Neutrality (= non-discrimination) on the other hand, can be regarded as both intentional and anintentional.

Neutrality (considered as an approximation —since absolute neutrality is non-existent) may only just be regarded as an end in itself. The same thing holds for intervention.

5.3.1.2. Typical Legislative Situations

5.3.1.2.1. Unintentional Neutrality

Repercussions are not intended, e.g. because the fiscal motive predominates ("rein fiskalisch"). Little or no consideration is given to possible secondary effects; at most, account will be taken of the possibility that overtaxation may entail loss of revenue.

We may talk of blind neutrality (when any secondary effects are unintentional and possibly even uncertain) in the same way as we talk of blind intervention (indifference to secondary effects).

It follows that blind intervention involves the risk of both intentional and unintentional discrimination, whereas blind neutrality can only entail unintentional discrimination,—or, of course, unintentional neutrality.

5.3.1.2.2. Intentional Neutrality

An attempt is made to neutralize repercussions by means of counteracting rules, possibly at the risk of losing revenue.

The best possible delimitation and the most precise definition of an intervention may frequently include the desire for neutrality in respect to conditions that are not to be affected.

5.3.1.2.3. Some Instances of Combinations

1) It is, e.g., easy to imagine a combination of intended external neutrality (TVA) and the intervention of Commen Market law (the double taxation resulting from refusing credit for entertainment expenses). The French call-

ed this treatment of entertainment expenses "puritan intervention" and refused to comply with the Brussels directive which does in fact, in its final version of 11th April 1967, make this provision optional to member states[11]).

2) The French have yet another curious instance to offer us: Prior to 1954 France had a so-called production tax, which only allowed "déduction physiques" (deductions for purchases of raw materials and subsidiary materials etc.), but not "déductions fiancières" (deductions for working plant and similar investment goods).

At that time there was a strong political desire to encourage investments.

I have been informed that the political desire to intervene in order to encourage investments was one of the fundamental motives underlying the introduction, in 1954, of a TVA allowing the investor or entrepreneur full and immediate credit for TVA paid on working plant and similar investment goods.

Not till later on did France build up a "philosophy": If TVA is desired to affect only the ultimate consumer (le consommateur final) and not the firm (l'entreprise), it follows that the firm should not be made to advance TVA payments on investment goods, i.e. that the firm should immediately be granted full credit for TVA paid on such goods.

The next phase is somewhat more clearly formulated; the "If" has been replaced by an "As": "As TVA is desired to ...".

Finally, it is stated that, in this way, TVA will be neutral in the situation: capital-intensive as opposed to labour-intensive methods of production. And so the philosophy becomes a "theory".

The phases of the development are illustrative:

(i) Prior to 1954 a purely fiscal production tax.

(ii) In 1954: deliberate intervention.

(iii) After 1954, and particularly during the discussions in Brussels: intentionally neutral seen in relation to the future.

In the Danish Report on the Tax on Value Added of 1964, Section 5 on page 102, the argumentation of the Common Market Commission is so formulated that the Commission might be suspected of being illogical. The Danish Report explains that the Commission recommends full and immediate credit for paid TVA as firms would otherwise have to be in advance with their TVA payments (i.e. the neutrality concept). The report concludes as follows: "The immediate credit for paid TVA is moreover easier to administer and encourages firms to invest". Obviously, a neutral tax should not offer any encouragement!

The difference between neutrality observed in relation to the past (neutralising intervention) and in relation to the future (abstraction from the past), being one of the fundamental distinctions, is so essential to a description of what is going on in Europe just now that a special section will be devoted to it: see below, Section 5.3.4.

5.3.2. Neutrality in Form versus Neutrality in Substance

Typically, neutrality in form will also be intentional. It is almost impossible to demonstrate neutrality in substance by scientifically reliable methods, especially when studying attempts to attain several different objectives at the same time. It will frequently be necessary to rely on approximations only.

5.3.2.1. Section 2 on page 31 of the Danish Report contains the following statement: "One of the ways in which it is sought to introduce neutrality is to see that the tax rate will be the same for all taxable consumer goods".

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11) See "Amtsblatt" of 14th April 1967, p. 1306, Article No. 11, (4).

A uniform tax rate, however, will only result in neutrality in substance in relation to prices and quantities provided the elasticity of demand is uniform. And there are of course great variations in the elasticity of demand; a circumstance from which excise duties benefit greatly, by the way. Moreover, the effect which a TVA with a uniform rate will have on a money economy will differ entirely from the effect it will have on a subsistence economy (e.g. agriculture).

It will readily be understood, however, that practical considerations restrict the possibilities of this situation to neutrality in form. And perhaps there will not be much harm in that. Neutrality in form only is a much greater problem in foreign trade (see below under Section 5.3.6.).

5.3.2.2. I shall now discuss a problem of internal neutrality in substance:

It is maintained that the models and concepts of macroeconomics and microeconomics are not so well integrated as they might be. The operational analysis, decision theories, motivation theories and communication theories of microeconomics may not have sufficiently changed the "economic man" of macroeconomics. At any rate, in the opinion of the present author as a jurist, the "economic man" should be subjected to a depth-psychological analysis, especially as regards the tax motive.

According to the idelogists in Brussels the full and immediate credit for paid TVA paid on investment goods is a manifestation of neutrality (neutrality in the allocation of resources).

A "rational" TVA-payer should not be tempted to effect the so-called "balance-sheet purchases", not even during a boom in sales. It is a general experience with regard to depreciation allowances in connection with direct taxation, however, that economically irrational "balance-sheet purchases" are so large that new legislation is called for. Such new legislation is in fact being prepared in Denmark at present.

The above comments are merely intended to suggest that the motivational neutrality principle may be more realistic in some situations than the principle of neutrality in the allocation of resources.

That the "psychologizing principle of motivational neutrality" is difficult to apply in practice appears from the Bill proposing an amendment of the Act on Depreciation Allowances already announced by the Danish Minister of Finance. The Bill provides for a reduction of the maximum 30 per cent allowance for depreciation of the book value of machinery etc. to 15 per cent in the first year. Conceivably, this provision may in fact either double or halve the risk of "balance-sheet purchases" (and accordingly the resulting distortions), depending on what the owner of the firm considers most important (to avoid tax or to obtain the largest possible income after tax in the long run according to a sober estimate—if he is primarily interested in avoiding tax he will have to double his "balance-sheet purchases").

5.3.3. Specific Neutrality versus General Neutrality

The problem may be considered in two ways; either as (1) the epistemological problem, or as (2) the problem of structuring norms.

5.3.3.1. The Epistemological Problem

P. Gersmann writes[12]): "Apart from actual discrimination, however, it is difficult to express any general opinion concerning the ultimate effect of the tax on the competitive capacity because it must be regarded as forming part of the over-all economic policy." Gersmann is presumably referring to the special discrimination mentioned by him ear-

12) "Revision og Regnskabsvæsen", 1966, p. 115.

lier in the same article. Gersmann concludes his comments on taxation of the profits of business firms as follows: "It is a theoretical as well as a practical problem how to find a satisfactory method for determining the impact of taxes on the relative competitive capacity of different countries."

On page 110 he points out: "... that such a harmonization (of tax rates as planned in the EEC) will raise the question of the part played by indirect taxes in the individual countries compared with direct taxes. If there are major variations between the different countries, it may easily become necessary to consider harmonizing the direct taxes too, and this will affect the fiscal freedom of action of the countries concerned."

In this connection I may mention that the EEC has issued a "Recommendation" to the effect that the stabilization policy of each individual member state is to be pursued by regulating government expenditure rather than by regulating taxes. It is asserted that this recommendation has been widely followed in practice. The EEC has therefore already given serious attention to the consequences which have also now been pointed out by Gersmann. The EEC is aware of the epistemological difficulties and their interrelatedness, and the problems are therefore being attacked over a broad front.

Epistemologically, therefore, we must pass from the specific to the general aspect, and, what is more, from taxes to ever larger and larger sectors of the economy.

5.3.3.2. The Problem of Structuring Norms

5.3.3.2.1. In General

Those who set the norms (legislators etc.) have two ways open to them: They may either try to trace the different possibilities of discrimination and then counteract them by nondiscriminatory rules, or they may formulate vague legal standards or omnibus clauses.

The Treaty of Rome uses both alternatives. According to Articles 95-98 it is forbidden to "play tricks" with export refunds, compensating duties or even with internal direct taxation to the prejudice of the other five member states. Article 99 is the section (promising future legislation) which has now resulted in a European TVA (which is to become operative not later than 1st January 1970).

If the omnibus clause is adopted, it is essential to know who is to implement the norm. Article 101 is a case in point:

"Where the Commission finds that a disparity existing between the legislative or administrative provisions of the Member States distorts the conditions of competition in the Common Market and thereby causes a state of affairs which must be eliminated, it shall enter into consultation with the interested Member States.

If such consultation does not result in an agreement which eliminates the particular distortion, the Council, acting during the first stage by means of an unanimous vote and subsequently by means of a qualified majority vote on a proposal of the Commission, shall issue the directives necessary for this purpose. The Commission and the Council may take any other appropriate measures as provided for in this Treaty".

The omnibus clause solves the problem of neutrality in two ways: In the first place, it constitutes a warning, an injunction to the member states to exercise caution and to act carefully (and that is perhaps the most important effect). In the second place, it authorizes the Commission and the Council to introduce a special kind of non-discrimination. It is probably no exageration to assert that neutrality in the EEC is of a special structural and institutional nature.

5.3.3.2.2. Harmonization

Harmonization must be said to strike the

balance between the specific and the general aspect.
The TVA model may be cited in this connection, since it constitutes a harmonization in form.
In direct taxation it is sought to harmonize the effects of taxation, that is for instance, the combination or result of the basis of assessment, tax rate, and the efficiency of taxation assessment, in short harmonization in substance. The following statement can be found on page 2 of "Dokument über die steuerliche Harmonisierung in der EWG für die Sitzung der Finanzminister" (Report on Tax Harmonization in the EEC for the Meeting of the Minister of Finance)[13]): "Secondly, it is appropriate and, incidentally, not difficult to formalize the harmonization of indirect taxes whereas this is more difficult, and possibly less imperative in respect to direct taxes; in the latter case the chief aim is to harmonize the effects; and this applies especially to taxes affecting the profits of firms and company dividends".
If there are major variations between member states, harmonization of the effects may occasionally be a more realistic solution. This may presumably be said to constitute a new variation on the theme: "neutrality in form versus neutrality in substance".
5.3.4. Neutrality Observed in Relation to the Past versus Neutrality Observed in Relation to the Future
5.3.4.1. As already mentioned under 5.3.1.2.3 2), the full and immediate right to credits for paid TVA on investment goods introduced by the French "taxe sur la valeur ajouté" in 1954 might be described as neutralizing intervention and at the same time as neutrality observed in relation to the future. Capital-intensive production methods were placed in a more favourable position than before and were therefore "encouraged". In addition, future neutrality was achieved in relation to labour-intensive production methods.
5.3.4.2. The most well-known instance of this approach to the problem is the EEC plan (Directive of 11th April 1967) to replace the Continental cumulative turnover taxes by TVA not later than 1st January 1970.
This neutralizing intervention introduces an innovation, viz. neutrality in the choice of consumer goods, in foreign trade, and in the structure of the business community, by abolishing double taxation (the cumulative elements) and by excluding the possibility of "playing tricks" at the frontier, or, to put it a little more cautiously: greater neutrality is achieved in the mentioned situations. This concrete example has been discussed and described so thoroughly that it is hardly possible to add anything new in this connection. Brief mention shall be made, however, of a transitional phenomenon described by H. Mesenberg[14]): The German export refunds (Ausfuhrvergütung) are at present being granted according to certain seemingly quite harmless average rates (Durchschnittssätze). However, Mesenberg has shown that the export industry is in fact the one which has achieved the greatest degree of integration, with the result that the cumulative element is of small consequence (export production is largely concentrated in the same giant combines). In this way the export industry is actually being granted a kind of export subsidy which will cease when TVA is introduced on 1st January 1968.
Besides, it is the angle of attack itself that is of general and permanent interest. The cumulative turnover tax will presumably disappear gradually also outside the EEC owing to the

13) EWG (15.056/IV/66-D) of 23rd November 1966.

14) Mehrwertsteuer und Aussenhandel", Institut Finanzen und Steuer, Bonn, October 1964.

pressure exerted by GATT and by international competition.

5.3.5. Neutrality of Direct Taxes versus Neutrality of Indirect Taxes.

5.3.5.1. It has already been mentioned under 5.3.3. that the EEC has achieved a harmonization in form of indirect taxes (TVA), and that the EEC is now primarily concerned with harmonizing the effects of direct taxes; more particularly the effects of the direct taxation of business.

5.3.5.2. It has also been mentioned above (2.9.) that indirect taxes affect prices directly through a shifting of the tax burden ("waren- oder preisbezogen" (relating to goods or prices), and that direct taxes affect the prices of goods and the competitive capacity indirectly (when taxes are "gewinnbezogen" (relating to profits) etc.).

It may be of some consequence to the structure of the business community, and the situation, establishment and dissolution etc. of a firm, if direct taxes affect overhead costs. If direct taxes affect variable costs (e.g., like a kind of gross tax), they will also affect prices. As there are innumerable types of direct taxes affect variable costs (e.g. like a kind of gross tax), they will also affect prices. As there are innumerable types of direct taxes—and it is indeed incredible how greatly even income taxes and company taxes may vary—it would appear to be a fairly difficult task to analyse the effects of the different direct taxes and then try to harmonize these effects. At the present time investigations and discussions are centering on taxation affecting capital movements and the concentration of firms across the frontiers. Another—and more powerful-instance of an attitude adopted by the EEC will be mentioned below under 5.3.6.3.2.2.

5.3.5.3. Qualification

Indirect taxes can be refunded on exports, whereas this is not the case with direct taxes. For this reason the qualification is important. It follows that, if a direct tax has practically the same effect on the distribution of the tax burden as TVA, it will prove worth while to abolish it, e.g. to increase the TVA to make up for the difference.

In some Common Market countries social charges are levied on firms in proportion to the wages or salaries paid to their employees, and these charges are therefore designated as parafiscal. If they were changed into fiscal taxes, e.g. by converting them into TVA, an advantage would be gained from an egoistical national point of view. German and Italian attempts at changing social "charges" into fiscal taxes have so far been rejected as inadequate—as being parafiscal.

5.3.5.4. The Dynamics of Neutrality Stemming from TVA

Structurally, TVA is actually something between a direct and an indirect tax. It is therefore the generally accepted view, based on the experience gained in France, that the introduction of TVA will sooner or later result in a merger of "direct taxes" authorities and "indirect taxes" authorities, and in this "organizational" way promote "the self-acting tendencies of harmonization".

5.3.5.5. Discordances Between TVA and Income Tax

A further question that may be posed is whether the expected merger of "direct taxes" authorities with "indirect taxes" authorities may be presumed to promote not only an external as well as an internal harmonization of tax administration but also of the direct and indirect taxes themselves, e.g., as regards the basis of assessment, whenever the two taxes overlap.

Examples:

5.3.5.5.1. Entertainment Expenses

The Danish TVA disallows credits for TVA paid on entertainment expenses, while these expenses are deductable in connection

with the assessment of income tax.
In so far as entertainment expenses can be established as working expenses, the Danish TVA results in double taxation and thereby in discrimination.
As mentioned above, joint administration of direct and indirect taxes has already been introduced in France. Consequently, France has adopted the same solution for TVA as for income tax, i.e. entertainment expenses are deductable, but deductions are restricted by natural skepticism. It has already been mentioned that, according to the latest EEC directive, and under the influence of the French argumentation, member states are left free to decide what measures to adopt in this respect.
5.3.5.5.2. Basis of Allowances for Depreciation
It is an old Danish tradition to disallow depreciation on office buildings for income tax purposes. The Danish TVA allows credits for TVA paid on such buildings for assessment purposes provided they have been erected by the firms for their own business activities. In this respect the Danish TVA appears to be more neutral than the Danish income tax.
5.3.5.5.3. Depreciation Period
As already mentioned, the Danish TVA allows full and immediate credit for paid TVA, the sole purpose being to impose tax on the ultimate consumer. Income tax is based on an entirely different kind of neutrality, viz. the greatest possible accuracy in the computation of the basis of taxation, including a "correct" allocation on income periods. This neutrality in the allocation of income periods dates from time when the income year was "sacrosanct". But the tradition appears to be deeply rooted. It was originally backed up by the demand for full progression in the fat years. The introduction of a proportional company tax in Denmark has weakened this argument.

The argument concerning "balance-sheet purchases" (the fear of distorting affects) may be presumed to affect both income tax and TVA from a point of view of motivational neutrality. The principles of neutrality in the allocation of resources do not provide the same clear answer in respect to direct taxes as they do in respect to indirect taxes.
Incidentally, as mentioned above under 3.1.1., the TVA introduced in Michigan is an "income tax type" of TVA which includes allowances for depreciation pro rata temporis.
5.3.6. External Neutrality versus Internal Neutrality
5.3.6.1. The Destination Principle does not Solve All the Problems.
Torben Jantzen, Danish Head of Department in EFTA's Secretariat in Geneva, writes in a feature article in the "Berlingske Titende" of 19th January 1967: "... the indirect taxes now levied in the EFTA countries are being studied in detail with a view to ensuring that the individual countries are imposing these taxes on imported goods and goods produced in the country concerned with the same amounts", cf. also Alban Hansen: "Problemer vedrørende harmonisering og tilpasning af indirekte afgifter i Fællesmarkedet og EFTA" ("Problems Relating to the Harmonization and Adjustment of Indirect Taxes in the European Common Market and EFTA") in "Nordisk Skattekonference i København i 1966" (Nordic Tax Conference in Copenhagen in 1966), ("Nordisk Udredningsserie", 1966: 4), page 22, 3rd paragraph.
Alban Hansen writes at the bottom of page 22 in connection with the destination principle: "In a way it may therefore be said that if the excise duties and turnover taxes—including the rules governing export exemptions and refunds—of member states are made non-discriminatory, it will in fact be unnecessary to harmonize these duties and taxes in order that a common market may

function satisfactorily. In fact, the EFTA provisions concerning the adjustment of indirect taxes do not impose obligations that are greater than those I have mentioned in the foregoing.

The Treaty of Rome, however, goes further than that...."

As far as I can see, Alban Hansen has not "in the foregoing" mentioned the intricate problems arising in connection with the choice of commodities liable to excise duty, e.g. wine and motorcars.

Portugal may, of course, "be glad that a uniform tax will be imposed in the Scandinavian countries on all wine produced south of Lisbon and north of Stockholm", but Portugal might conceivably go further in its reasoning on the subject neutrality, even though this reasoning may not find formal support in the EFTA Convention.

The Danish purchase tax on motor-cars is probably the highest of its kind in the Western World. There are no motorcar factories in Denmark—only assembly plants and marketing and service organizations. It is quite conceivable that the United Kingdom and Sweden will likewise argue in favour of making "some allowances" for the country of origin.

Portugal's vindication of wine is already in full swing. So here is a new variation on the theme: neutrality in form versus neutrality in substance.

5.3.6.2. TVA secures the optimum "legal" export refunds, and may for that very same reason result in paradoxes of neutrality, at any rate for a time.

5.3.6.2.1. The Period Preceding the Harmonization of Rates of Taxation (a uniform rate for all goods in all EEC countries):

Each individual member state will be able to obtain a competitive advantage over the other member states by being the first to introduce TVA and the first to increase the rate of taxation to the level agreed upon for the harmonization of taxes, say 17 per cent. It would be possible to reach this high percentage, e.g. by converting part of the excise duties into TVA.

5.3.6.2.2. In the period following harmonization of the rates of taxation the state in which the revenue from TVA constitutes the largest share of total revenue from taxation will presumably—all other things being equal—obtain an advantage.

This is an intricate problem, however.

5.3.6.2.3. According to GATT's rules, TVA also secures optimum export refunds. What has been mentioned under 5.3.6.2.1., therefore, also applies in the relationship between the Common Market and third-party countries and may therefore acquire more lasting importance.

The paradox would seem to be that the neutral TVA may for a time be used as an egoistically national competitive device by one member state of the EEC against the other member states or by the EEC against third-party countries.

What has just been mentioned above might be used to supplement Alban Hansen's comments at the bottom of page 22 (see above under 5.3.6.1., 3rd paragraph).

5.3.6.3. Questions Concerning Neutrality Asked at Brussels:

5.3.6.3.1. Supposing that some company taxes and a large part of the excise duties are shifted on to TVA in order to secure larger export refunds and thereby a better position in the international competition,

1) What "legal" possibilities will the EEC then have of reacting against such a step?

The answer was: None today.

Unanimity in the Council of Ministers would of course solve this problem too (Articles 99, 101 and 102). So far, however, member states have shown a strong preference for tax autonomy.

2) Is it actually likely that the EEC, being strongly in favour of TVA, will react at all:
A) If faced with a fait accompli before entering into negotiations for admission?
B) If the question is raised during the negotiations?
C) If the question is raised after the application for membership has been filed?
The answer was: The EEC will then courteously recommend that the balance between direct and indirect taxes should be maintained on an approximate fifty-fifty basis, and that the levying of taxes on business should be used as the principal range of measurement, since this would be in accordance with the EEC's present long-term objectives.
5.3.6.3.2. The problem might be further formulated so as to comprise the whole structure of taxation or the relation between the different types of taxes, including proposed taxes, positive versus negative taxes, etc.
Rules (liberal) governing allowances for depreciation and company taxes (low) may readily be used as nationally egoistic competitive devices. Our Danish company tax, for instance, is one of the lowest in Western Europe.
May we exercise sovereignty in respect to negative taxes:
1) in the form of personal grants (to maintain the social balance)?
2) in the form of grants in connection with purchases of, e.g., machinery (instead of granting generous allowances for depreciation, c.f. the British way of presenting the problem in "Investment Incentives", London 1966, H.M.'s Stationery OfficeC mnd. 2874)?
The answers were: 1) will be respected; 2) will only be respected to a very limited extent (for details see Article 92). Moreover, this whole complex of problems is still being studied and discussed.

6. THE "NEUTRALITY" OR LACK OF NEUTRALITY OF THE MARKET GROUPINGS SEEN IN RELATION TO TAX STRUCTURES

What has so far been said seems to indicate that, irrespective of whether the other countries ("third-party countries") like TVA or not, they will have to introduce it, either on being formality admitted as members of the EEC or because the international competition on "legal optimum export refunds" compels them to do so. Denmark may be the first instance of this state of affairs, but it will hardly be the last.
It has previously been mentioned that the Common Market has planned, or has already initiated, a series of investigations concerning specific problems of direct taxation. The results of these investigations, and the ensuing deliberations, directives, resolutions of the Council of Ministers etc., will in time be likely to entail very considerable changes in the Danish tax structure.
This whole complex of problems therefore requires the utmost attention and calls for intensive research; the latter possibly—and prefcrably—by cooperation between the Nordic countries. We may learn quite a lot from the EEC about the advantages of cooperation and the splitting up of the work in this field.

7. INTERVENTIONISM OF COMMON MARKET LAW

It would be interesting to see if the influence which the EEC exerts on the Danish tax system will generate interventionist elements, e.g. Common Market law rules intended to stimulate economic growth (incentive taxation).
The endeavours of the EEC have so far been directed exclusively towards eliminating the fiscal "Wettbewerbsverzerrungen" (distortions of competition). It has not ventured to tackle the problems of the "Dirigisme" of

Common Market law. Marjolin speaks cautiously of "programmation". It is, of course, only a question of differences in degree.
The "Dokument über die steuerliche Harmonisierung..." mentioned under 5.3.3.2., however, contains the following statement at the bottom of page 3:

"The coordination of the fiscal policies of member states, and the imposition of taxes as a means of economic intervention, shall simply be secured within the framework of Common Market policy and in line with the over-all policy pursued within certain fields."

DR. ERWIN SPIRO:

THE REASONS BEHIND THE BUDGET 1967-8 (SOUTH-AFRICA)

The Budget speech of the Minister of Finance Dr. Dietrich has now been implemented by the Income Tax Act, 1967 (Act No. 95 of 1967). The question may well be asked: What are the reasons behind it?

Dr. Dietrich made the words: "work and save" his motto, but also referred to a renewed determination in the struggle against inflation. Elsewhere he explained that the promotion of productivity was one of the most important weapons in the battle against inflation and that saving was one of the pillars upon which the Budget rested. How do the new taxation measures tally with these principles?

INCOME TAX ON COMPANIES

The main burden of the additional R106.2 million income tax falls on the companies. In the view of the Minister of Finance many of them made large profits, and the rate of company tax—which will now amount to 40% of taxable income—is very moderate in comparison with that in other countries. Companies, except gold and diamond mining companies, will now pay, instead of 33⅓% plus a loan levy of 1⅔%, altogether 35%, 36⅔% and 3⅓% loan levy, altogether 40% of taxable income. Gold and diamond mining companies will pay a further loan levy of 5% on tax. Companies mining for oil will pay on each rand of taxable income derived from mining for natural oil excluding gas 50c whereas they have to pay 40c if such taxable income is derived from mining natural oil in the form of gas; the tax may be reduced to or by such an amount as the Minister of Mines in consultation with the Minister of Finance may determine.

INCOME TAX ON INDIVIDUALS

As regards individuals who are liable for central government income tax of R100 or more, the loan levy has been increased from 5% to 15%. This increase should not hit the taxpayer too severely as he can recover the loan levy in more normal times.

NON-RESIDENT SHAREHOLDERS' TAX

The non-resident shareholders' tax has been increased from 10%, to which it was increased last year, to 15%. According to Dr. Dietrich, this rate is nearer to the average rate levied by other countries; it will also be deducted from the tax which such shareholder pays in his own country.

NON-RESIDENTS TAX ON INTEREST

The non-residents tax on interest is a new tax on interest accruing to persons not ordinarily resident in the Republic or to the deceased estate of persons who at the date of their death were not ordinarily resident in the Republic or to companies not registered in the Republic, provided the debtor is ordinarily resident or carries on business in the Republic. The rate is ten per cent. It does not matter whether the interest is from a source in the Republic (or deemed to be in the Republic)—which attracted tax under the old Act—or from a source outside the Republic, although in the former case the new tax is deductible. Dr. Dietrich pointed out that interest on loans concluded outside the Republic was regarded as being derived from a source outside the Republic and up to now tax free, notwithstanding the fact that such interest might be deducted from the taxable income of the South African borrow-

er as allowable expenditure. Also, as Dr. Dietrich mentioned further, the new tax would in many cases be deductible from the tax which the non-resident had to pay in his own country. An amount accruing to a shareholder in a building society out of the profits of such society is deemed to be interest. The Act provides, however, for eight exemptions of which three may be briefly mentioned.

In the first instance, interest accruing from the Government (including the Railway Administration and any provincial administration), a local authority, the Electricity Supply Commission and the South African Reserve Bank is exempted.

In the second instance, interest on money borrowed by the debtor outside the Republic will be exempt if the Secretary for Inland Revenue is satisfied-

(a) that such money has not been borrowed for the purpose of producing gross income, that the payment of the interest and the repayment of the money will be made outside the Republic out of funds derived by the debtor entirely outside the Republic and not out of his resources in the Republic or

(b) that such money was borrowed by the debtor in the ordinary course of a trade carried on by him outside the Republic and was not specifically intended to be used by the debtor for the purpose of producing gross income.

In the third instance, interest on bills of exchange and promissory notes will be exempt to the extent that such interest is payable in respect of the purchase price of goods imported into the Republic, if such instruments are handled through a banking institution under the Banks Act, No. 23 of 1965, or the South African Reserve Bank and either certifies thereon that a bill of lading or other document covering the importation of such goods has been exhibited to it.

The debtor has to deduct or withhold the tax and must pay it to the Secretary within fourteen days after the date of accrual of the interest, submitting at the same time a declaration in the prescribed form.

CONCESSIONS

Undistributed Profits Tax

The exemption from undistributed profits tax on the ground that not less than fifty per cent of the equity share capital were held throughout the specified period by non-residents (if the latter were companies, provided they derived the greater portion of their income from sources outside the Republic) has been extended to include the proportionate part of the shares held by persons so qualified through private companies not so qualified.

Exporters' Allowance

As large increases in the production of gold could no longer be expected, Dr. Dietrich appealed to exporters to spare no effort to capture overseas markets. To provide the necessary incentive, the exporters' allowance has been increased in the case of the basic allowance from 25% to 37½% and in the case of the enhanced allowance from 37½% or 50% to 50% or 62½% respectively, in other words in each instance by 12½%.

Smoothing of Fluctuations in Farming Income

A farmer may enjoy an unusually high income in one year, but such year may be followed by years of adversity caused by the vicissitudes of the elements. To come to the farmer's assistance, provision is now made for the averaging of the rates of normal tax chargeable, provided the farmer elects to avail himself of this facility. Normally a period of five years will be taken into account,

and there is a special rating formula. If a farmer has made the election, the special rating formulas in respect of drought and disease, plantation income and income from the disposal of sugar cane as a result of fire do not apply. The rating formula in respect of lump sum benefits from pension, provident and retirement annuity funds is likewise not applicable whereas the benefits of the rating formula in respect of husband and wife are not excluded.

The election must be made within a certain time and in the prescribed form and, once made, is binding for succeeding periods of assessment, except in the case of a woman whose income is subsequently deemed to be her husband's as the result of marriage.

Parents

The rebate in respect of university students available to parents has been increased by extending the maximum age from 24 to 26 26 years.

As a relief in regard to the expenses connected with the birth of a child an additional rebate of R8 has been allowed in the year in which a child is born, as has also the maximum deduction for medical expenses in that year been increased from R200 to R300.

CONCLUSION

It is impossible to apply to the various taxation measures set out above one and the same principle. "Work and save" is appropriate as regards the increase of the loan levy portion of the tax, but the adequacy of the phrase must be doubted when the increase of the company tax (other than the loan levy portion) is considered. It may, however, be argued that such increase of tax still assists in the battle against inflation in that companies are left with less of their profits. But by no stretch of imagination can it be said that the new non-residents tax on interest and the increase of the rate of non-resident shareholders' tax are of an anti-inflationary nature. They simply attract more revenue.

Apart from the extension of the exports' allowance which is clearly meant as an incentive to export more, the various concessions serve the purpose of alleviating certain hardships.

In the concluding part of the Budget Speech the Minister of Finance posed the question whether it was not desirable to introduce a measure of flexibility by empowering the Government to raise or lower certain tax rates or loan levies within prescribed limits, subject to confirmation by Parliament at the first opportunity thereafter. According to the Minister, such power existed or was proposed in certain other countries; he made, however, no proposal in this direction. It is considered that the present "inflexibility" is to be preferred.

C. CHAUVIN :

NOTE SUR LA FISCALITE MALGACHE

Le Code Fiscal Malagasy, inspiré de la fiscalité française, comprend trois branches bien distinctes :

A – Les impôts directs et indirects,
B – Les droits d'enregistrement et timbre,
C – Les droits de douane.

Les impôts directs sont divisés à leur tour en plusieurs catégories que nous allons énumerer et analyser sommairement. L'impôt sur les bénéfices divers dû sur les bénéfices ou revenus provenant des entreprises commerciales, industrielles, artisanales, des exploitations agricoles, minières, des professions libérales, ainsi que de toutes occupations, exploitations lucratives et sources de profits non soumises à un impôt cédulaire spécial sur le revenu, à l'exception des salaires, pensions et rentes viagères.

Le bénéfice net imposable est déterminé par les recettes provenant d'opérations de toute nature effectuées par les entreprises, sous déduction des frais généraux pour la période correspondante; des charges financières (rémunérations payées aux capitaux investis); des moins values sur réalisations; des amortissements; de certaines provisions justifiées.
Le taux de cet impôt est uniformément de 16% pour les entreprises particulières et de 31% pour les sociétés de capitaux. Une réduction pour charge de famille est accordée aux entreprises particulières, qui ne peut excéder 4.000 FMG par enfant.

Des allégements fiscaux sont accordés aux particuliers qui investissent sur le Territoire sous la forme :

- d'acquisitions de terrains à bâtir (construction à réaliser dans un délai de trois ans) ;
- d'acquisition de terrains en friche pour mise en valeur, dans un délai de six ans ;
- construction et extension d'immeubles à l'usage d'habitation, agricole, industriel et minier ;
- acquisition de gros matériel aux usages ci-dessus ;
- construction, installation présentant un caractère éducatif ou sanitaire.

La déduction accordée sur les bénéfices imposables est égale à 85% en ce qui concerne les investissements agricoles, égale à 50% en ce qui concerne les autres investissements, du montant des investissements effectués par l'entreprise.
Les pertes de l'entreprise pendant un exercice sont reportables jusqu'à épuisement, sur les cinq exercices suivants.
Les sociétés étrangères ayant un établissement sur le Territoire sont soumises, pour ce qui concerne cet établissement, aux mêmes règles que les entreprises dont le siège est à Madagascar.
Dans ce cas la quote part des frais généraux du siège incombant à l'établissement est admise en déduction des bénéfices.
Des régimes préférentiels adaptés à chaque cas sont étudiés pour les entreprises apportant un essor important, à l'économie du Territoire.
L'impôt sur les bénéfices n'est pas déductible des bénéfices net imposables.
L'impôt général sur le revenu est dû sur tous les revenus de quelque nature qu'ils soient s'ils ne sont pas exonérés par une disposition particulière.
Cet impôt frappe les revenus :
des propriétés foncières bâties ;
des valeurs et capitaux mobiliers ;
du commerce et de l'industrie ;
des exploitations agricoles et minières ;
des professions libérales, charges et offices ;

des emplois des secteurs public et privé;
retraites, pensions et rentes viagères;
et en général les revenus de tous capitaux et de toutes occupations lucratives.
Les avantages en nature des emplois sont fixés forfaitairement à 4% pour le logement et à 2% pour les autres avantages du montant brut des émoluments.
Une diminution de 15% est accordée aux salaires titulaires d'un contrat de travail d'expatrié.
Une diminution dégressive de 15 à 10% est également comptée sur les salaires au titre de frais professionnels.
Les revenus locatifs diminués forfaitairement de 30%.
En outre sont déduits des revenus imposables: les intérêts sur emprunts; tous les impôts et taxes assimilés payés par le contribuable pour l'exercice intéressé; les versements de primes d'assurance sur la vie humaine, à concurrence de 10% des revenus avec un maximum de 40.000 FMG augmentés de 10.000 FMG par enfant à charge.

Là aussi des exonérations sont prévues pour les sommes déposées à la Caisse d'Epargne, les souscriptions aux actions ou parts sociales de certains organismes agréés par l'Etat; les investissements effectués sur le Territoire, sous la forme de construction d'immeubles, d'achat de terrain en friche et la mise en valeur de ces terrains.
Le total des sommes ainsi épargnées et investies est déduit du revenu net imposable dans la limite de 25% de ce revenu.
Le reliquat des sommes épargnées et investies peut être reportée sur les trois années suivantes dans la même limite que ci-dessus.
L'impôt sur le revenu se compose:
a – d'une cotisation fixe établie en fonction du revenu net imposable, progressive et allant de
1.000 FMG pour les revenus allant de 90.000 à 99.000 FMG jusqu'à
37.000 FMG pour les revenus de 2.500.001 et supérieurs.
b – d'une cotisation établie en fonction du revenu net imposable calculée ainsi:

4	%	sur la fraction des revenus allant de					90.000	à	100.000	FMG
5	%	,,	,,	,,	,,	,,	101.000	à	180.000	,,
6,5	%	,,	,,	,,	,,	,,	181.000	à	400.000	,,
10	%	,,	,,	,,	,,	,,	401.000	à	600.000	,,
13,5	%	,,	,,	,,	,,	,,	501.000	à	800.000	,,
17	%	,,	,,	,,	,,	,,	801.000	à	1.000.000	,,
20,5	%	,,	,,	,,	,,	,,	1.001.000	à	1.250.000	,,
23	%	,,	,,	,,	,,	,,	1.251.000	à	1.500.000	,,
26,5	%	,,	,,	,,	,,	,,	1.501.000	à	1.750.000	,,
30	%	,,	,,	,,	,,	,,	1.751.000	à	2.250.000	,,
33	%	,,	,,	,,	,,	,,	2.251.000	à	3.000.000	,,
40,5	%	s/les fractions des revenus supérieurs à 3.000.000								

Déductions. Les contribuables mariés ont droit, sur leurs revenus, de 40.000 FMG augmentés de 40.000 FMG par enfant à charge.
Majorations. 25 à 30% pour les contribuables du sexe masculin célibataires, veufs ou divorcés qui n'ont pas d'enfant.
15% pour les contribuables du sexe masculin mariés depuis plus de deux ans et qui n'ont pas d'enfant.

Taxes sur les bénéfices commerciaux non réinvestis à Madagascar.
Cette taxe est due par toute personne morale ou physique assujettie à la contribution des patentes, et dont l'activité est classée dans la catégorie "commerce".
La taxe est établie chaque année sur la différence entre le bénéfice et le total formé par la rémunération aux taux de 12% du capital investi, d'une part, et d'autre part, par les investissements effectués ou provisionnés.
La partie de cette différence inférieure ou égale à 3.000.000 FMG n'est pas imposée;
La partie comprise entre 3.000.001 FMG et 5.000.000 FMG est comptée pour $\frac{1}{3}$ de sa valeur;
La partie comprise entre 5.000.001 et 10.000.000 FMG est comptée pour $\frac{1}{2}$ de sa valeur;
La partie supérieure à 10.000.000 de FMG est intégralement comptée.
Le bénéfice visé ci-dessus est celui qui sert de base à l'impôt sur les bénéfices divers établi au titre de la même année, avant les déductions prévues pour investissements, mais sous deduction ici, de l'impôt sur les bénéfices divers dû au titre de l'année précédente.
Le taux de la taxe est fixé à 25%. Il est ramené à 15% pour les entreprises des particuliers ou en nom collectif.
Taxe sur les transactions. Cette taxe est due par toutes les personnes physiques ou morales qui, habituellement, achètent pour revendre.
Sont taxables sous cette forme, les ventes mobilières, immobilières, les fournitures de marchandises ou de services, à l'exception des professions libérales.
Toutefois les opérations d'assurances sont soumises à la taxe.
Sont également taxables les affaires traitées par des personnes n'ayant pas d'établissement à Madagascar mais vendant des marchandises à des détaillants ou aux consommateurs par l'intermédiaire de personnes établies dans le Territoire. Dans ce dernier cas la taxe est établie au nom de l'intérmédiaire.
Les personnes dont les ventes ou fournitures annuelles taxables sont égales ou inférieures à 3.000.000 FMG;
Les personnes dont les fournitures de service taxables sont d'un montant égal ou inférieur à 900.000 FMG (1.500.000 FMG pour les transporteurs) sont éxonérées de la taxe.
Les produits de première utilité: Riz, lait, pain, sel, farine, produits d'exploitation de fermes, etc. ne sont pas soumis à la taxe.
Le taux de la taxe est fixé à 2% sur la généralité des affaires et à 4% pour les opérations d'assurances, de banques, de spectacles ainsi que pour les ventes au détail effectuées directement par les grossistes ou demi grossistes.
La taxe est payable par trimestre échu sur déclarations établies par le contribuable et versée au Trésor.
Les trois impôts et taxes ci-dessus doivent faire l'objet de déclarations déposées le 28 février de chaque année pour les entreprises dont l'exercice social se termine au cours du premier semestre de l'année précédente, et le 31 mars de chaque année pour celles dont l'exercice social se termine pendant le deuxième semestre.

FISCALITE TRADITIONNELLE

La fiscalité traditionnelle comprend:
– La contribution des patentes est due par toute personne morale ou physique de nationalité Malagasy ou étrangère exerçant à Madagascar un commerce, une industrie, un métier ou une profession.
La patente se compose
a– d'un droit fixe par la nature de l'activité

exercée, le nombre de salariés occupés et le chiffre de la population du lieu d'activité.
b– d'un droit proportionnel établi en fonction de la valeur locative des locaux professionnels, et éventuellement de celle de l'outillage utilisé.
La patente est dûe non pas par profession, mais par établissement, c'est à dire pour chaque point d'activité appartenant à une même entreprise.
L'impôt du minimum fiscal, impôt de capitation égal pour tous les assujetis d'un même district. Il est fixé à 2.500 Frs par personne. Cet impôt vise un but socio-économique en obligeant les paysans qui constituent la grande masse de la population à travailler davantage et à commercialiser leurs produits.
– L'impôt sur les bovins est dû par toute personne à raison des animaux de race bovine agés de plus d'un an qu'elle possède.
Le tarif unitaire est fixé chaque année par le Conseil de Province, ou communal de la région en cause.
Le taux en cours est de 100 FMG par tête de bovin.
– L'Impôt Foncier
Cet impôt est dû sur tous les terrains occupés à titre de propriétaire, de concessionnaire ou d'occupant effectif.
Cependant les terrains nouvellement mis en culture et constituant une extension effective de la surface cultivée ne sont imposés qu'à partir de la sixième année qui suit celle de la mise en valeur, et de la dixième année pour les terrains reboisés présentant une densité minimum de 1500 arbres vivants à l'hectare. Le taux de l'impôt est fixé de 5 à 700 FMG par hectare suivant la catégorie et la situation de ces terrains.
– L'impot sur la propriété bâtie dû par toute personne à raison des locaux d'habitation, commerciaux et industriels dont elle est propriétaire ou occupant effectif, mais qui ne sont pas soumis à la taxe sur les propriétés bâties, perçues au profit d'une commune urbaine.
Sont exemptés pendant les dix années qui suivent leur achèvement les constructions nouvelles, reconstructions et extensions répondant aux nécessités de l'hygiène moderne et de l'urbanisme.
Ces locaux sont imposés:
a– pour les maisons d'habitation en quatre catégories suivant le nombre de pièces.
b– pour les locaux commerciaux et industriels suivant la valeur locative et du matériel fixe.
Taux de l'impôt=
– a) Locaux d'habitation (au maximum par construction)

	Agglomération de plus de 2000 habitants	Agglomération de 500 à 2000 habitants	Agglomération de moins de 500 habitants
Première catégorie	500 FMG	200 FMG	100 FMG
Deuxième catégorie	800 ,,	500 ,,	250 ,,
Troisième catégorie	1.600 ,,	1.000 ,,	500 ,,
Quatrième catégorie	3.200 ,,	2.000 ,,	1.000 ,,

– b) Locaux commerciaux et industriels: Taux de 5% au maximum.

– L'Impôt sur les armes à feu rayées ou non possédéés par le contribuable: Taux= 1.000 FMG au maximum par arme.

TAXES COMMUNALES

	Taux et Tarifs	
	Maxima	Minima
1° Taxe sur la propriété bâtie:		
– à usage d'habitation ou autres locaux;	12%	6 %
– à usage de profession libérale ou de commerce;	15%	8 %
– à usage d'industrie ou de métier;	10%	5 %
2° Taxe sur la propriété non bâtie	1%	0,5%
3° Taxe de balayage et d'enlèvement des ordures ménagères	5%	3 %
4° Taxe de désinsectisation	2%	1 %
5° Taxe de déversement à l'égout	2%	1 %
6° Taxe s/ les chiens (par animal)	1.000 FMG	
7° Taxe sur les véhicules (par cheval vapeur fiscal taxable).	1.000 FMG	

CENTIMES ADDITIONNELS

Il pourra être établi au profit des budgets des Chambres de Commerce des centimes additionnels à la contribution des patentes perçue dans les districts sur lesquels s'étend la compétence de la Chambre de commerce bénéficiaire.

Le taux maxima des centimes additionnels mis à la disposition des budgets des Chambres de Commerce est fixé comme suit:

– Centimes additionnels à la contribution des patentes: 20%.

Réclamations. En cas de désaccord, les réclamations doivent être déposées, suivant des imprimés prévus à cet effet, dans les six mois de la mise en recouvrement.

Dans le cas où la réclamation serait rejetée en tout ou partie, le contribuable peut avoir recours à la Cour Suprême en dernier ressort.

La Fiscalité Malagasy recherche les modalités pouvant assurer une garantie aux investissements étrangers sur le Territoire. Elle doit, en même temps satisfaire son but naturel qui est la juste rentrée des impôts.

Jeune encore, elle s'adapte chaque année, aux nécessités de l'heure, et en raison de l'évolution économique rapide du pays, elle subira certainement de nouvelles modifications dans les détails de son application avant de trouver une stabilité durable.

BOMCHIL PINHEIRO CLARO LAVALLE & BADO:

RECENT TAX MODIFICATIONS IN ARGENTINA*)

Argentinian Government has just established laws which bring modifications to some federal taxes.

Those modifications have reduced assessment and are in harmony with the general stabilization policy and economical development to which are tending the measures taken by the Government at the present time.

So, the first ones which are going to be commented, are those established by lawn no. 17.330 promulgated on the 6th of July 1967. They stated tax reductions for the agrarian and industrial fields as well as some exemptions in the matter of stamp tax, internal and inheritance taxes.

The same law abolishes a tax which had just been recently created and commented in this Bulletin for Fiscal Documentation no. 5, Page 195). This one consisted in a 2% assessment on loans.

I

1) In order to make easy transactions, originated out of Argentina, it has been decided:

a) The complete elimination of the tax on benefit produced by credits obtained abroad, when their purpose was to finance imports for industrial equipment. That is to say, that the foreign moneylender will not have to pay any tax in Argentina when the money which he gave had been used for financing industrial equipments imports in Argentina.

b) In the specific case of financial loans from abroad, without any consideration of the employment of the money, the tax has been reduced to the half.

c) In case of payment made by Argentina to abroad in relation with technical assistance or fees, the tax also has been reduced to the 50%.

2) Some tax measures have just been taken by the Government tending to help Argentinian meat exportation. They are reflected in the law we comment.

a) A variable index from 15 to 30% is established in concept of deduction from income tax of the first sales of male bovines.

b) It is also allowed to deduct money amounts used to by female bovines.

c) Can be deducted also from the amount to be paid in concept of annual income tax, expenses to buy products against pleagues or to kill weeds. This deduction is allowed separately from the ones of general caracter which may be appliable to the tax payer.

d) Moreover, those exploitations dealing with land and cattle may deduced—from the income tax to be paid—half of the amount paid to professionnal experts in matters specialized to increase land production.

e) Land exploitation may deduced also from income tax amount to be paid, the total of the investment in pasture grounds, animal kept for breeding purpose, housing for the personal and any other investment made in order to improve the rural production.

3) An important measure has been taken also to improve local industrial production.
Industry can deduced 50% of the amounts invested in the purchase of machines and equipment of Argentinian production.

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*) This article is a follow-up to the articles in the March and May 1967 issue of the Bulletin and prepared under the direction of "Le Cabinet Juridique Spécialisé en Droit Sud American à Paris, Bomchil Pinheiro Claro Lavalle & Bado."

4) With the purpose of helping to solve an actual problem of the wine production which consists in the lack of wine containers, wines productors will be authorized to deduce the total invest in the purchase of such containers.

5) Important measures have been taken to make easy reduction of interest rate and help in general the financial money market. In fact, 2% assessment on loans which was established last March has been abolished.
Additionally, stamp tax rate is reduced to the half in case of exchange operations.

II

Another tax modification has been stated on the 29th of July last. It consists in a reduction of the income tax in case of housing investments.
Decree no. 5376/67 has rewarded article 154 of the Income Tax Law no. 11.682. Now the taxpayer will be able to deduce from the annual income tax, the half of the amounts invested in housing whose caracteristics of superficies and other are in accordance with decree dispositions.
As it can be seen, that is a fiscal measure taken in order to make easy the construction of economical houses and to contribute to solve the housing problem in Argentina.

III

The third tax modification that we consider necessary to comment is the new fiscal revaluation law that has been issued by the Government on July 10, which law is registered under the number 17.335.
In countries with a high annual inflation percentage, the renewal of assets represented like real estate and equipment produces a very difficult problem for the tax payer. What fiscal legislation allows in general is to amortize equipment for instance under a percentage of its purchase price. But in high level inflation countries, purchase price of the same equipment will be much higher than the original one and in consequence, practically impossible for the tax payer to renew it with the amortization percentage foreseen by the law.
To solve the problem and to help in general local industry, the Argentinian Government issued the commented law that allows now to amortize assets in a percentage that is calculated on an amount that is the original purchase price multiplied by a coefficient that varies from 1 (in case of assets purchased, built or produced in 1967) to 147 for assets that appeared in 1944 balance sheet.
The new law substitutes the former one about fiscal revaluation, no. 15.272 that was issued in 1960 and passed out of date as the inflation process still went on. New dispositions foreseen to help balance sheet to show the reality of each enterprise, helping also the economical activities to pay taxes not on capital but calculated on authentical benefits.
Now, each enterprise will have the real possibility to renew industrial equipment and assets in general. Argentinian Government published an information through which officials had calculated that tax collection will be reduced in about 2.000 millions of Argentinian pesos on the next 10 years but such effort had been considered necessary to help the development of private economy.
New regulations are in force for company fiscal year closed between June 13th 1967 and June 29th 1968.
However the new law is not compulsory for tax payers but optional.

* * * * DOCUMENTS * * * *

VORSCHLAG EINER

RICHTLINIE DES RATES DER EWG

ÜBER EINE GEMEINSAME METHODE ZUR BERECHNUNG DER IN ARTIKEL 97 DES VERTRAGES VORGESEHENEN DURCHSCHNITTSSÄTZE

(Von der Kommission dem Rat am 30 Juni 1967 vorgelegt)*

Der Rat der EWG,
gestützt auf den Vertrag – insbesondere auf die Artikel 99 und 100,
gestützt auf den Beschluss der im Rat versammelten Vertreter der Regierungen der Mitgliedstaaten vom 21.6.60,
gestützt auf den Vorschlag der Kommission,
gestützt auf die Stellungnahme des Parlaments,
gestützt auf die Stellungnahme des Wirtschafts- und Sozialausschusses in Erwägung nachstehender Gründe:

Seit Inkrafttreten des Vertrages hat die Festlegung der in Art. 97 des Vertrages vorgesehenen Durchsschnittsätze zum Ausgleich der Belastung durch die Umsatzsteuern, die nach dem System der kumulativen Mehrphasensteuer erhoben werden, fortwährend Schwierigkeiten hervorgerufen, die dem ordnungsmäßigen Funktionieren des gemeinsamen Marktes abträglich sind; diese ungünstigen Auswirkungen werden sich mit fortschreitendem Wegfall der Binnenzölle in der Gemeinschaft noch verstärken.

Diese Schwierigkeiten beruhen vor allem auf den Unterscheiden zwischen den in den Mitgliedstaaten für die Berechnung der gegenannten Durchschnittssätze verwendeten Methoden.

Eine Harmonisierung dieser verschiedenen Methoden liegt deshalb im Interesse des Gemeinsamen Marktes. Sie geschieht durch die Annahme gemeinsamer Berechnungsregeln, welche die Beachtung der in Art. 97 gesetzten Obergrenze sicherstellen und eine Nachprüfung der auf diese Weise errechneten Sätze erlauben.

Um möglichst weitgehend die tatsächlichen Produktionsverhältnisse einer Ware oder Gruppe von Waren zu berücksichtigen, müssen die Vorschriften eine Gewichtung der verschiedenen Steuerbelastungen vorsehen.

Bei der Berechnung der Steuerbelastung einer Ware auf ihren verschiedenen Produktionsstufen sollten aus Gründen der technischen Vereinfachung nur die sich nenneswert auf die Belastung auswirkenden Elemente festgehalten und die anderen durch pauschale Zuschläge abgegolten werden.

Die Berechnungsvorschriften müssen darüber hinaus den Mitgliedstaaten die Möglichkeit lassen, bestimmte pauschale Festsetzungsverfahren zu wählen;

Et ist zweckmäßig, die Kommission zu ermächtigen, nach Konsultation der Mitgliedstaaten Ausführungsvorschriften für die gemeinsame Berechnungsmethode zu erlassen;

Um der Kommission ihre Aufgabe zu erleichtern, die Beachtung der durch den Vertrag

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*) Richtlinie ohne Begründung veröffentlicht im Amtsblatt der Europäischen Gemeinschaften 201/1967.

bestimmten Obergrenze für die Durchschnittssätze zu überwachen, ist es notwendig vorzusehen, daß die Mitgliedstaaten vor der Neueinführung und Änderung von Durchschnittssätzen der Kommission von sich aus die nach der Gemeinsamen Methode durchgeführten Berechnungen vorlegen;
hat folgende Richtlinie erlassen:

Artikel 1
Wird von einem Mitgliedstaat auf Grund des Art. 97 des Vertrages ein Durchschnittssatz eingeführt oder geändert, der sowohl bei der Einfuhr als auch bei der Ausfuhr die inländische Umsatzsteuer ausgleichen soll, die unmittelbar oder mittelbar die Herstellung einer Ware oder Gruppe von Waren belastet, so darf dieser Satz den entsprechenden Satz der durchschnittlichen Umsatzsteuerbelastung nicht übersteigen, die für diese Ware oder Gruppe von Waren gemäß den Artikeln 2 bis 8 festgelegt wurde. Diese Belastung muß nach Maßgabe der tatsächlichen wirtschaftlichen Produktionsbedingungen berechnet werden.

Artikel 2
Die durchschnittliche Belastung einer Ware entspricht dem gewogenen Mittel der Belastungen auf den typischen Produktionswegen der Ware. Die Belastung auf jedem Produktionsweg wird gemäß Art. 3-6 festgestellt. Das gewogene Mittel wird nach dem Anteil jedes Produktionsweges an der Gesamtproduktion der Ware gebildet.
Die durchschnittliche Belastung einer Gruppe von Waren entspricht dem gewogenen Mittel der durchschnittlichen Belastung der für die Gruppe typischen Waren. Die Zahl der zu untersuchenden typischen Waren richtet sich nach dem Umfange der Gruppe von Waren. Für jede typische Ware wird die durschschnittliche Belastung gemäß Abs. 1 tern, die Beachtung der durch den Vertrag festgestellt. Das gewogene Mittel wird nach dem Anteil der einzelnen typischen Waren und der von ihnen vertretenen Waren an der Gesamtproduktion der Gruppe von Waren gebildet.

Artikel 3
Für die Berechnung der Belastung einer Ware auf der letzten Produktionsstufe können die Belastungen folgender Kostenfaktoren berücksichtigt werden:
Rohstoffe, halbfertige Erzeugnisse, Fertigwaren, Hilfsstoffe, Verpackungsmaterial, Veredelungsarbeiten, Investitionen und von Dritten durchgeführte Transporte.
Neben diesen Kostenfaktoren können einzelne Kostenelemente bei der Berechnung der Belastung ebenfalls berücksichtigt werden, wenn der Anteil jedes Elements am Verkaufspreis – Steuer ausgenommen – mindestens 5% beträgt.

Artikel 4
1. Für die Berechnung der Belastung einer Ware auf der ersten Vorstufe werden die Belastungen der Kostenfaktoren Rohstoffe, halbfertige Erzeugnisse und Fertigwaren berücksichtigt, soweit sie einmal in den Rohstoffen, halbfertigen Erzeugnissen und Fertigwaren der letzten Produktionsstufe enthalten sind, zum andern soweit sie in den anderen berücksichtigungsfähigen Faktoren und Elementen der letzten Produktionsstufe enthalten sind, und deren Anteil am Endverkaufspreis – Steuer ausgenommen – mindestens je 5% beträgt.
2. Für die Berechnung der Belastung einer Ware auf den weiteren Vorstufen können nur die Belastungen der Kostenfaktoren Rohstoffe, halbfertige Erzeugnisse und Fertigwaren berücksichtigt werden, die in die Rohstoffe, halbfertigen Erzeugnisse und Fertigwaren der letzten Produktionsstufe eingehen.

3. Darüber hinaus kann die Belastung jedes gemäß Art. 3 auf der letzten Produktionsstufe berücksichtigten Kostenfaktors oder – elements pauschal um 10% erhöht werden.
Beruht jedoch die Belastung eines Kostenfaktors oder – elements auf der Anwendung eines speziellen Umsatzsteuersatzes, so ist die Belastung für die Anwendung der Pauschalerhöhung vorher auf der Grundlage des Normalsatzes neu zu berechnen.

Artikel 5

1. Wird für einen Kostenfaktor oder ein Element der letzten Produktionsstufe auf die Berechnung der berücksichtigungsfähigen Vorbelastung gemäß Art. 4 verzichtet, so kann die Belastung des betreffenden Kostenfaktors oder -elements pauschal um 5% erhöht werden.
Beruht jedoch die Belastung des Kostenfaktors oder -elements auf der Anwendung eines speziellen Umsatzsteuersatzes, so ist die Belastung für die Anwendung des Pauschalzuschlages vorher auf der Grundlage des Normalsatzes neu zu berechnen. Gilt der spezielle Umsatzsteuersatz einen oder mehrere Vorumsätze ab, so ist ein Pauschalzuschlag nicht zulässig.
2. Die derart berechnete Belastung für die Vorstufen darf jedoch diejenige nicht übersteigen, die sich bei der Anwendung der Art. 4 und 6 für den betreffenden Kostenfaktor oder das Element ergeben würde.

Artikel 6

1. Besteht für einen berücksichtigungsfähigen Kostenfaktor oder ein Kostenelement – gleichgültig auf welcher Stufe – bereits ein Durchschnittssatz, so kann er für die Berechnung der Vorbelastung dieses Faktors oder Elements insoweit übernommen werden, als er mit Artikel 97 vereinbar ist. Die Anwendung eines solchen Satzes ist zwingend, soweit gemäß Artikel 10 der Kommission Berechnungen zur Begründung dieses Satzes vorgelegt wurden.
2. Die Anwendung eines solchen Satzes auf einen Faktor oder ein Element auf der letzten Stufe schließt jede pauschale Erhöhung der Belastung dieses Faktors oder Elements aus.

Artikel 7

1. Wird auf die Berechnung der durchschnittlichen Belastung einer Ware oder einer Gruppe von Waren gemäß Art. 2-6 verzichtet, so kann diese Belastung pauschal auf 100%, 75% oder 35% des Normalsatzes der Umsatzsteuer geschätzt werden, je nachdem, ob die berücksichtigungsfähigen Faktoren und Elemente auf der letzten Produktionsstufe der Ware oder Gruppe von Waren, die dem Normalsatz oder einem erhöhten Umsatzsteuersatz unterlegen haben, mindestens 65%, 50% oder weniger als 50% des Verkaufspreises der Ware oder der Gruppe von Waren – Steuer ausgenommen – betragen.
2. Die derart geschätzte Belastung darf die durchschnittliche Belastung nicht übersteigen, welche sich bei Anwendung der Art. 2-4 und 6 ergeben würde.

Artikel 8

Die Durchschnittssätze sind auf halbe Prozent auf- oder abzurunden, je nachdem, ob der Bruchteil des errechneten Satzes 0,25% bzw. 0,75% erreicht oder nicht.

Artikel 9

Ausführungsvorschriften zu den Art. 1-8 werden, soweit erforderlich, durch Richtlinien der Kommission nach Anhörung der Mitgliedstaaten erlassen.

Artikel 10

1. Beabsichtigt ein Mitgliedstaat die Einführung oder Änderung eines Durchschnittssatzes, legt er der Kommission die nach Art.

1-8 durchgeführte Berechnung der durchschnittlichen Belastung vor.
2. Ist die Kommission der Auffassung, eine gemäß Art. 5 oder 7 pauschal geschätzte Belastung übersteige die in den Art. 5 Abs. 2 und Art. 8 Abs. 2 festgesetzte Grenze, legt der Mitgliedstaat der Kommission auf ihr Verlangen die nach Art. 2-4 und 6 durchgeführte Berechnung dieser Belastung vor.

Artikel 11
Die Mitgliedstaaten setzen die Kommission unverzüglich von den Gesetzen, Verordnungen oder Verwaltungsvorschriften in Kenntnis, die sie zu erlassen haben, um den Vorschriften dieser Richtlinie Folge zu leisten.

Artikel 12
Die Mitgliedstaaten tragen dafür Sorge, daß der Kommission der Wortlaut der wesentlichen Vorschriften des innerstaatlichen Rechts mitgeteilt wird, die sie später auf dem von dieser Richtlinie betroffenen Rechtsgebiet erlassen.
Diese Richtlinie ist an die Mitgliedstaaten gerichtet.

BEGRÜNDUNG

I. ALLGEMEINES

Seit Inkrafttreten des EWG-Vertrages hat Artikel 97 zu zahlreichen Schwierigkeiten geführt, da er von den einzelnen Mitgliedstaaten verschieden angewandt wird; selbst der Begriff des Durchschnittssatzes wird nicht einheitlich ausgelegt. Im übrigen unterscheiden sich die für die Höhe der Ausgleichsabgaben geltenden Berechnungsmethoden in den einzelnen Ländern voneinander, woraus sich zusätzliche Schwierigkeiten für eine Kontrolle der Durchschnittssätze gemäß Art. 97 ergeben.
Die gemeinsame Berechnungsmethode will diesen Schwierigkeiten abhelfen. Im Rahmen des Art. 97 will sie gewährleisten, daß die Durchschnittssätze der Ausgleichsteuern bei der Einfuhr und der Rückvergütungen bei der Ausfuhr die in diesem Artikel gesetzten Grenzen nicht überschreiten.
Die gemeinsame Methode zwingt jedoch nicht, bei der Festsetzung der Sätze bis an die Obergrenze zu gehen. Ein Mitgliedstaat könnte z.B. seine Sätze nur auf 50% des zulässigen Höchstsatzes festsetzen. In einem solchen Fall müßte diese Handhabung allerdings gleichmäßig bei allen Erzeugnissen Platz greifen, für die Ausgleichsteuer- und Rückvergütungssätze bestehen; würde ein Staat diese Regel nicht beachten, so verstiesse er gegen den Beschluß der im Rat versammelten Vertreter der Regierungen der Mitgliedstaaten vom 21.6.1960 ("in der Regel sollen Änderungen der Ausgleichsteuern und Rückvergütungen aus wirtschafts-, handels- und währungspolitischen Gründen nicht vorgenommen werden") und eventuell auch gegen die Art. 101 und 102 des Vertrages, da sich aus solcher ungleichmässigen Anwendung Verzerrungen ergeben können.
Um zu vermeiden, daß mit den Ausgleichsteuern und Rückvergütungen wirtschafts-, handels- und währungspolitische Zwecke verfolgt werden, ist – ebenfalls gemäß des Beschlusses vom 21. Juni 1960 – davon auszugehen, daß die Sätze der Ausgleichsteuern und Rückvergütungen in der Regel gleich sein sollten. Es bestehen jedoch keine Bedenken, daß in besonders zu begründenden Ausnahmefällen für ein gleiches Erzeugnis bei der Ausfuhr ein Rückvergütungssatz zugebilligt wird, der niedriger ist als der entsprechende Ausgleichsteuersatz. Diese Abweichung erscheint erforderlich um zu vermei-

den, daß ein Staat ggf. gegen Artikel 96 des Vertrages verstößt, wenn er einen höheren Betrag erstattet als die tatsächliche Belastung; dieser Fall könnte eintreten, wenn die Ausfuhren einer Ware im wesentlichen von integrierten Unternehmen vorgenommen werden.

In technischer Hinsicht unterscheidet sich die vorgeschlagene Methode in ihren großen Linien kaum von dem in den Mitgliedstaaten bereits angewandten Verfahren: Zerlegung der Ware auf der letzten Produktionsstufe in ihre verschiedenen Bestandteile, wobei anschliessend jeder einzelne Bestandteil wiederum zerlegt wird. Vom Ausgangspunkt "Ware" werden deren Bestandteile immer weiter zurück verfolgt; eine Begrenzung auf bestimmte Stufen ist nicht vorgesehen.

Dieses Zerlegungsverfahren bringt jedoch Schwierigkeiten mit sich, welche die Methode letztlich unanwendbar machen könnten. Sehr rasch vervielfältigt sich beim Zurückgehen auf die Vorstufen die Zahl der Bestandsteile und deren Elemente, die Erfassung ihres Wertes wird immer ungenauer und ihr Einfluss auf die Steuerbelastung des Endprodukts immer geringer. Deshalb erschien es angebracht, nur eine bestimmte Zahl von Bestandteilen (Faktoren und Elemente) bei der Berechnung der Belastung zu berücksichtigen und zum Ausgleich bestimmte Pauschalzuschläge vorzunehmen.

Da im übrigen die kumulative Mehrphasensteuer Unterschiede der Steuerbelastung einer Ware vor allem als Folge der unterschiedlichen Integration der Herstellungsbetriebe mit sich bringt, schien es außerdem zweckmäßig, für die Ermittlung der Durchschnittssätze aus den einzelnen festgestellten Belastungen auf verschiedenen Produktionswegen das gewogene Mittel zu bilden.

Obwohl diese Berechnungsmethode im allgemeinen ohne große Schwierigkeiten angewandt werden kann, schien es doch nützlich – besonders im Hinblick auf eine Vereinfachung des Verfahrens – auch pauschale Zuschläge und Sätze vorzusehen. Die Anwendung dieser Pauschalen dürfte im wesentlichen wohl zu den gleichen Ergebnissen führen wie die eingehende Berechnungsmethode.

Unter Steuerbelastung einer Ware wird die Belastung durch die Umsatzsteuer bei der Herstellung der Ware oder Gruppe von Waren auf den verschiedenen Produktionsstufen verstanden. Die Belastung der Handelsstufen nach der Herstellung der auszuführenden Ware wird durch die Methode nicht erfasst. Hierfür kann deshalb einem Ausfuhrhändler eine zusätzliche Vergütung gewährt werden. Andererseits darf die dem Ausfuhrhändler darüber hinaus gewährte Vergütung für die Belastung der ware bei ihrer Herstellung nicht höher sein als die Vergütung, die der selbst exportierende Hersteller erhalten würde.

Die einzelnen Belastungen können auf Preise bezogen werden, die die Steuer einbeziehen oder ausschliessen. Der gewählte Bezugspreis muß dann jedoch allen Berechnungen zugrunde gelegt werden.

II. ERLÄUTERUNGEN DER ARTIKEL

Artikel 1

Der Artikel stellt die Methode in den Rahmen des Art. 97 des Vertrages und stellt Regeln für die Berechnung der Steuerbelastung auf. Er betont die Notwendigkeit, der Festsetzung der Ausgleichsteuer- und Vergütungssätze die tatsächlichen Produktionsverhältnisse zugrunde zu legen, und schließt damit gleichzeitig jede Berechnung auf der Grundlage hypothetischer Wirtschaftsstrukturen oder Unternehmen aus.

Wird indessen eine bestimmte Ware oder Warengruppe im Inland nicht erzeugt, so können für eine Extrapolation Substitutionserzeugnisse herangezogen werden.

Artikel 2

Zur Berechnung der Durchschnittssteuerbelastung eines bestimmten Erzeugnisses ist es erforderlich, seine verschiedenen Produktionswege zu untersuchen, wobei innerhalb eines Produktionsweges auch die auf diesem Wege üblichen Handelsstufen berücksichtigt werden können.

Aus der technischen und strukturellen Verschiedenheit der Produktionswege ergeben sich unterschiedliche Verkaufspreise und Belastungen. Nach der Wirtschaftsstruktur werden im allgemeinen drei hauptsächliche Typen vorkommen: die Ware wird durch aufeinanderfolgende nicht integrierte, durch teilweise integrierte oder durch voll integrierte Unternehmen hergestellt. Die untersuchten Produktionswege sollten die gesamte Produktion einer Ware erfassen. Das nach dem Anteil jedes Produktionsweges an der Gesamtproduktion berechnete gewogene Mittel der Belastungen ergibt den Durchschnittssatz.

Die Zuordnung der Produktion zu den einzelnen Typen wird nicht in jedem Fall eindeutig erfolgen können; da die Schwierigkeiten in jedem Mitgliedstaat etwa gleich groß sind, wird erst die praktische Anwendung der Vorschrift ergeben, welcher Spielraum im einzelnen möglich und notwendig ist.

Soll die durchschnittliche Belastung einer Gruppe von Waren festgestellt werden, können nur Waren ähnlicher Art, deren Steuerbelastung im wesentlichen gleich ist, in einer Gruppe von Waren zusammengefaßt werden. Soweit diese Voraussetzungen gegeben sind, können die in der Unterteilung einer Zolltarifposition zusammengefaßten Waren eine Gruppe bilden.

Innerhalb jeder Gruppe werden die einzelnen Waren verschiedenen Waren zugeordnet, die als repräsentativ für diese Untergruppe angesehen werden können. Richtunggebend hierfür können steuerliche Gründe (gleiche Belastung) und technische Gründe (ähnliche Produktionsbedingungen) sein.

Zuerst wird die durchschnittliche Belastung der ausgewählten, für die Gruppe typischen Waren nach den vorstehend genannten Regeln berechnet; anschließend erfolgt eine Gewichtung dieser Belastung je nach dem Anteil der einzelnen typischen Waren und der von ihnen vertretenen Untergruppe an der Gesamtproduktion der Gruppe (gewogenes Mittel).

Das folgende schematische und theoretische Beispiel erläutert die anzuwendende Methode der Gewichtung:

Es sei von einem bestimmten Erzeugnis ausgegangen, dessen Verkaufspreis je Einheit auf der Herstellerstufe

400 – im Repräsentativunternehmen des Produktionsweges 1

460 – im Repräsentativunternehmen des Produktionsweges 2

500 – im Repräsentativunternehmen des Produktionsweges 3 beträgt.

Der Betrag der in jedem dieser Produktionswege angefallenen Umsatzsteuerbelastung sei jeweils

16 – 20,70 – 24,

was in Verhältnis zum Verkaufspreis folgenden Vomhundertsätzen entspricht: 4% – 4,50% – 4,80%.

Im übrigen macht

– der Produktionsweg 1

50% der Inlandsproduktion,

– der Produktionsweg 2

30% der Inlandsproduktion,

– der Produktionsweg 3

20% der Inlandsproduktion aus.

Dementsprechend hätte eine erste Gewichtung zu erfolgen, um den Durchschnittsverkaufspreis je Einheit im Inland zu ermitteln, sodann eine zweite Gewichtung zur Ermittlung der entsprechenden durchschnittlichen Umsatzsteuerbelastung.

– Durchschnittlicher Verkaufspreis je Einheit:

$$\frac{400\times 50}{100}+\frac{460\times 30}{100}+\frac{500\times 20}{100}=\ 438$$

– Durchschnittliche Umsatzsteuerbelastung:

$$\frac{16\times 50}{100}+\frac{20{,}70\times 30}{100}+\frac{24\times 20}{100}=\ 19{,}01$$

Der Durchschnittssatz ist demzufolge:

$$\frac{19{,}01\times 100}{438}=\ 4{,}34$$

Bestimmte Mitgliedstaaten ziehen es vor, die Berechnungen ausschließlich in Vomhundertsätzen darzustellen.

In diesem Falle ist in dem obrigen Beispiel die Ausgangsbasis 100 gleich dem Verkaufspreis des in dem Repräsentativunternehmen des Produktionsweges 1 hergestellten Erzeugnisses. Für die beiden anderen Produktionswege sind die entsprechenden Werte:

Produktionsweg 2: $\frac{460}{400}=\ 112$

Produktionsweg 3: $\frac{500}{400}=\ 125$

Die Steuerbelastung für jeden der drei Produktionswege errechnet sich dann wie folgt:

1. Produktionsweg: $\frac{4\times 100}{100}=\ 4$

2.Produktionsweg: $\frac{4{,}50\times 112}{100}=\ 5{,}175$

3.Produktionsweg: $\frac{4{,}80\times 125}{100}=\ 6{,}00$

Die erste Gewichtung ergibt den Durchschnittsverkaufspreis je Einheit (immer auf der Basis 100):

$$\frac{100\times 50}{100}+\frac{112\times 30}{100}+\frac{125\times 20}{100}=\ 109{,}50$$

Die zweite Gewichtung bestimmt die Durchschnittssteuerbelastung:

$$\frac{4\times 50}{100}+\frac{5{,}175\times 30}{100}+\frac{6\times 20}{100}=\ 4.7525$$

Der Durchschnittssatz ist demzufolge:

$$\frac{4{,}7525\times 100}{109{,}50}=\ 4{,}34\%$$

Artikel 3

Bei der Berechnung der steuerlichen Belastung einer Ware wird unterschieden werden müssen zwischen der Belastung der letzten Produktionsstufe, der vorletzten Stufe und jeder der Vorstufen.

Unter der Belastung einer Stufe sind die Steuern zu verstehen, die unmittelbar die auf dieser Produktionsstufe verwendeten Güter und Dienstleistungen belastet haben.

Artikel 3 behandelt die Berechnung der Belastung der letzten Stufe.

Die in Absatz 1 festgehaltenen berücksichtigungsfähigen Kostenfaktoren dürften im allgemeinen die wichtigsten Belastungen der Ware auf dieser Stufe erfassen. Von anderen Kostenfaktoren können zusätzliche Kostenelemente berücksichtigt werden, die eine gewisse finanzielle Bedeutung haben (5%-Klausel).

Unter "Kostenfaktor" wird eine bestimmte, nach betriebswirtschaftlichen oder kaufmännischen Gesichtspunkten zusammengefaßte Gruppe einzelner Kostenelemente verstanden. So stellen z.B. allgemeine Unkosten kein Kostenelement dar, sondern einen Kostenfaktor, der sich aus einer Anzahl von Elementen, wie Reklame, Versicherungen usw. zusammensetzt.

Unter "Investitionen" sind alle Wirtschaftsgüter zu verstehen, die der Abnutzung unterliegen. Bestimmend für die Auslegung sind die allgemeinen steuerlichen Abschreibungsvorschriften; steuerliche Sonderabschreibungen können jedoch im allgemeinen nicht berücksichtigt werden.

Artikel 4

Dieser Artikel behandelt die Berechnung der Belastungen auf den Vorstufen.

Er sieht ein dem Artikel 3 entsprechendes Berechnungsverfahren vor, jedoch werden grundsätzlich nur noch die Faktoren Rohstoffe, halbfertige Erzeugnisse und Fertig-

waren berücksichtigt. Auf der ersten Vorstufe ist noch eine Ausnahme zugelassen: es können auch die Belastungen anderer Faktoren und Elemente berücksichtigt werden, da sie auf dieser Stufe noch einige Bedeutung für das Endergebnis haben können.
Zum Ausgleich für die Belastung der auf der ersten und den weiteren Vorstufen nicht berücksichtigungsfähigen Kostenfaktoren und -elemente besteht die Möglichkeit, die Belastung aller Faktoren und Elemente pauschal um 10% zu erhöhen. Ausgenommen sind die gemäß Art. 5 pauschal um 50% erhöhten Belastungen, sowie die Belastungen, die durch Übernahme eines bereits bestehenden Satzes gemäß Art. 6 berechnet wurden; in diesen Fällen ist davon auszugehen, daß alle Vorbelastungen bereits berücksichtigt sind. Beruht die Belastung eines Faktors oder Elements auf der Anwendung eines anderen als des Normalsatzes (Pauschalsatz, erhöhter Satz, ermässigter Satz, Umsatzsteuerfreiheit), wird der Pauschalzuschlag von 10% auf eine Belastung berechnet, die sich bei der Anwendung des Normalsatzes ergeben würde. Es ist davon auszugehen, daß die früheren Umsätze dem Normalsatz unterworfen waren.

Artikel 5

Es bleibt den Mitgliedstaaten unbenommen, auf die Berechnung der Belastung der Vorstufen zu verzichten. In diesem Falle besteht die Möglichkeit, die Belastung der Vorstufen pauschal auf 50% der Belastung der Endstufe zu schätzen. Diese Pauschalerhöhung ist jedoch nur insoweit zulässig, als die einzelnen Faktoren und Elemente auf der ersten Vorstufe berücksichtigt werden können.
Die pauschale Erhöhung wird als Abgeltung der gesamten Belastung auf den Vorstufen des betreffenden Faktors oder Elements angesehen. Die gemäß Art. 4 vorgesehene Pauschalerhöhung von 10% ist deshalb nicht gleichzeitig mit der Pauschale von 50% anwendbar. Absatz 2 weist darauf hin, daß die Pauschale eine Erleichterung für den Mitgliedstaat sein soll, daß sie aber nicht zu einem höheren Satz führen darf, als sich gemäß Art. 4 ergeben würde.

Artikel 6

Es bleibt den Mitgliedstaaten schon jetzt unbenommen, von Art.6 in größerem Umfange Gebrauch zu machen. Sie können bei Einführung der Gemeinsamen Methode bereits bestehende Sätze übernehmen, wenn sie mit Artikel 97 des Vertrages in Einklang stehen.
Es ist darauf hinzuweisen, daß Art. 6 die gesamte Vorbelastung des Bestandteils einer Ware betrifft, aber auch nur die Vorbelastung. Der Erwerb des Bestandteils selbst für die weitere Verarbeitung fällt nicht unter Art. 6; die Belastung dieses Erwerbsvorgangs ist gesondert festzustellen.
Da dieser Satz sämtliche Belastungen der Vorstufen einschließt, entfallen alle Pauschalerhöhungen, wenn er auf der letzten Produktionsstufe angewandt wird. Wird dagegen ein bestehender Durchschnittssatz auf einen Faktor oder ein Element auf einer der Vorstufen angewandt – was voraussetzt, daß auf die Anwendung des Art. 5 verzichtet wird – dürfte die Pauschalerhöhung von 10% gemäß Art. 4 Abs. 3 zulässig sein, da nur teilweise dieselbe Belastung doppelt erfasst wird und die Auswirkungen gering sind.
Ein bestehender Satz ist auch dann anwendbar, wenn ein auf einer Stufe berücksichtigungsfähiger Faktor oder ein Element nicht über diese Stufe hinaus berücksichtigt werden kann.
Die Gründe, die für eine Nichtberücksichtigung dieser Faktoren und Elemente über eine bestimmte Stufe hinaus (Art. 3 und 4) sprechen, nämlich die Kontrollschwierigkeiten, die sich aus ihrer weiteren Berücksichtigung ergeben würden und das Streben

nach Vereinfachung dürften in diesem Falle nicht mehr stichhaltig sein, da es sich um Faktoren oder Elemente handelt, deren Steuerbelastung bekannt ist.
Hieraus ergibt sich, daß z.B. Verpackungsmaterial, das auf der letzten Stufe mit 3% im Preis enthalten ist, auf der ersten Vorstufe berücksichtigt werden kann, wenn bereits ein Durchschnittssatz besteht, obwohl es normalerweise gemäß Art. 4 Abs. 1 nicht berücksichtigt werden kann.
Ebenso kann, wenn z.B. Verpackungsmaterial auf der letzten Stufe mit 12% im Preis enthalten ist, und ein Durchschnittssatz für dieses Verpackungsmaterial nicht besteht, normalerweise nur die Belastung der Rohstoffe, halbfertigen Erzeugnisse und Fertigwaren, die im Verpackungsmaterial enthalten sind, gemäß Art. 4 Abs. 1 letzter Halbsatz berücksichtigt werden. Die Vorbelastung dieser Bestandteile dagegen ist nicht zu berücksichtigen (Art. 4 Abs. 2). Besteht jedoch ein Durchschnittssatz, so kann er auf diese Rohstoffe, halbfertigen Erzeugnisse und Fertigwaren, die im Verpackungsmaterial enthalten sind, angewandt werden.

Artikel 7

Aus Gründen der Vereinfachung soll den Mitgliedstaaten die Möglichkeit eröffnet werden, auf jede Berechnung der Belastung einschließlich der Berechnung des gewogenen Mittels zu verzichten und sie statt dessen pauschal zu schätzen. Diese Pauschalen können sowohl auf Gruppen von Waren als auch auf einzelne Waren angewandt werden. Das unter Art. 2 zum Begriff "Gruppe von Waren" Gesagte gilt auch hier.
Da die Pauschalsätze einer mittleren Belastung Rechnung tragen sollen, mußten sie so festgesetzt werden, daß sie normalerweise nicht zu Beanstandungen Anlaß geben.
Die Einschränkung in Absatz 2 soll gewährleisten, daß die durch die Methode näher bestimmte Obergrenze nicht überschritten wird.

Artikel 8

Nach der in den Mitgliedstaaten allgemein geltenden Regelung schien es zweckmäßig, die Sätze in Abständen von 0,5% festzusetzen.

Artikel 9

Bei den Besprechungen mit Regierungssachverständigen sind zahlreiche Einzelfragen aufgetaucht, die nicht ohne weiteres den einzelnen Bestimmungen der Methode zugeordnet werden konnten Bei der außerordentlichen Vielgestaltigkeit der Materie schien es zweckmäßiger, in der Richtlinie selbst nur die Grundsätze aufzunehmen, die Regelung der Einzelfälle jedoch späteren Ausführungsbestimmungen zu überlassen.

Artikel 10

Artikel 10 legt die Verpflichtung der Mitgliedstaaten fest, der Kommission die zur Begründung neuer oder geänderter Sätze dienenden Berechnungen vorzulegen.

Die Kommission behält sich indessen das Recht vor, die Belastung auf der Grundlage der Art. 2-4, unbeschadet ggf. des Art. 6, zu überprüfen, wenn die Sätze halb-pauschal (Art. 5) oder völlig pauschal (Art. 8) ermittelt wurden, da diese Pauschalermittlung als Erleichterung für die Mitgliedstaaten gedacht ist, die jedoch nicht auf kosten der Richtigkeit gehen darf.

XXI CONGRESS OF I.F.A. – STOCKHOLM – 1967

RESOLUTION

(Deuxième sujet*)

I LE CONGRES:

NOTE AVEC SATISFACTION la recommandation du Conseil de l'Organisation de Coopération et de Développement Economiques (OCDE) de 30 Juillet 1963 demandant aux Pays Membres de poursuivre leurs efforts en vue de conclure des conventions bilatérales tendant à éviter les doubles impositions et de se conformer à cet effet au Projet de Convention élaboré par l'OCDE;

NOTE EGALEMENT que, dans les conventions conclues ou amendées postérieurement à 1963, de nombreux Etats se sont inspirés de la définition donnée à l'établissement stable par ledit Projet de Convention (article 5);

CONSTATE qu'il existe ainsi à l'heure actuelle, en matière de conventions internationales, une définition usuellement acceptée de la notion de l'établissement stable, ce à quoi visait la recommandation essentielle formulée par le XIè Congrès de l'IFA tenu à Vienne en 1957;

II LE CONGRES:

EXPRIME L'ESPOIR qu'afin de sauvegarder l'harmonisation atteinte grâce aux travaux de l'OCDE, les délégations en présence ne modifieront la définition type de l'OCDE lors de l'élaboration de nouvelles conventions que dans le cas où des conditions particulières, existant dans les rapports entre les Etats en présence, l'exigeraient laissant à l'O.C.D.E. le soin de procéder aux adaptations et améliorations qui s'avéreraient utiles.

EST D'AVIS que les critères retenus par le Comité Fiscal de l'OCDE, pour qu'un établissement stable soit constitué dans un pays, tiennent compte d'une manière équitable des intérêts des Etats en présence, tout en étant de nature à promouvoir les relations économiques sur le plan international;

ESTIME NOTAMMENT que c'est à juste titre que la définition de l'établissement stable donnée par le Comité Fiscal a innové en la matière, en excluant de la définition de l'établissement stable les lieux d'affaires utilisés aux fins de publicité, de fourniture d'informations, de recherches scientifiques ou d'activités analogues ayant un caractère préparatoire ou auxiliaire;

RELEVE TOUTEFOIS, sur la base des rapports soumis au congrès que les mêmes termes ne sont pas toujours interprétés d'une manière identique dans les divers pays, en particulier en ce qui concerne les formes d'activités qui ne sont pas génératrice d'établissements stables;

CRAINT que par l'incertitude qu'elle est susceptible d'entrainer, cette situation ne soit de nature à faire perdre aux exceptions prévues par l'OCDE une partie de leur importance pratique, l'absence de règles précises – lesquelles devraient être uniformes pour éviter la double imposition – étant de nature à constituer une source de conflits latents et à dissuader les contribuables de se prévaloir desdits exceptions;

DEMANDE EN CONSEQUENCE aux Administrations intéressées de publier chaque fois que cela sera possible, les décisions rendues,

*) L'évolution dans les différents pays du concept d'établissement stable, notammant du point de vue de l'harmonisation dans les futurs accords sur la double imposition.

ainsi que les directives qu'elles seraient amenées à établir en vue d'interprêter la définition donnée au terme d'établissements stable par les conventions internationales;
RAPPELLE aux Administrations intéressées la possibilité offerte par le chiffre 9 du Commentaire de l'OCDE ad. art. 25, suggérant un recours consultatif au Comité Fiscal dans le cas de difficultés spéciales se rapportant à l'application des conventions et exprime l'espoir qu' il sera fait usage de la possibilité ainsi offerte;
RAPPELLE EN OUTRE les résolutions prises par les Congrès de l'IFA de Zurich en 1951, de Vienne en 1957 et de Bâle en 1960, concernant l'institution d'une juridiction internationale en matière fiscale;
EST D'AVIS que la doctrine serait en mesure de jouer un rôle utile en étudiant plus en détail la portée qu'il convient d'attribuer aux diverses exceptions à l'application de la définition de l'établisssement stable formulées par l'OCDE et exprime en consequence l'espoir qu'une étude systématique du problème puisse être entreprise sur une plan international dans ce domaine.

III EN OUTRE, LE CONGRES:

EST DE L'OPINION qu'un progrès ultérieur en matière de définition uniforme de la notion de l'établissement stable est possible dans le cadre d'accords multilatéraux, tels qu'ils sont à l'étude au sein de divers organismes internationaux et exprime l'espoir que la définition de l'établissement stable donnée dans ces accords tiendra compte de la tendance actuelle des entreprises à décentraliser leurs activités sur un plan international et s'abstienne d'élever des obstacles à une telle décentralisation, dans la mesure où ceci ne serait pas commandé par des considérations impérieuses d'ordre fiscal;
RECONNAIT que l'imposition des entreprises ayant une activité dans plusieurs pays pose des problèmes particuliers aux pays en voie de développement en sorte qu'il conviendra d'apporter certains aménagements à la définition standard de l'établissement stable dans le cas de conventions conclues avec ces pays; estime toutefois qu'une harmonisation de la définition de l'établissement stable est souhaitable dans ce cas également et exprime en consequence le voeu que des travaux soient entrepris par un organisme international en vue de l'élaboration d'une définition uniforme, tenant équitablement compte des intérêts des Etats en présence tout en encourageant les relations économiques sur le plan international.

IV LE CONGRES PAR AILLEURS:

SUGGERE AU COMITE FISCAL DE L'OCDE de procéder notamment à un examen des points suivants en vue de formuler le cas échéant des recommandations ou précisions complétant son rapport de 1963:
1) à en juger d'après les rapports nationaux la pratique des differents Etats paraît être d'admettre l'existence d'un établissement imposable dès qu'un agent dépendant sans pouvoir de conclure dispose d'un lieu fixe d'affaires doté de certains moyens matériels, ce qui pourrait être en contradiction avec la position adoptée par l'OCDE selon laquelle un tel agent peut disposer de stocks d'exposition ou de livraison sans qu'il en résulte de conséquences fiscales;
2) ni le projet de convention de l'OCDE, ni le Commentaire ne mentionnent expressément les cas des services après vente souvent maintenus dans un pays par une entreprise étrangère, en sorte qu'il paraît y avoir parfois incertitude quant à la possibilité d'assimiler cette forme d'activité commerciale à une activité auxiliaire ne constituant pas un établissement stable, surtout si le personnel

technique dispose d'un stock de pièces de rechange;

3) le cas des centres régionaux dispensant du know how ou de l'assistance technique pourrait utilement faire l'objet d'une précision tendant à éliminer les incertitudes actuelles, en établissant clairement dans quelle mesure l'exonération accordée par le projet de l'OCDE sera affectée par le fait que l'objet principal de l'entreprise est de fournir du know how, de l'assistance technique ou d'autres prestations analogues, à des tiers à titre onéreux ou par l'importance de l'activité déployée par l'entremise du centre par rapport à l'activité de l'entreprise dans son ensemble.

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EDITORIAL:

TAX HAVEN CAYMAN ISLANDS

It might be useful to call attention to the Cayman Islands, which may become a desirable new base for foreign companies. The Cayman Islands, which were prior to 1959 a dependency of Jamaica, are now a British colony. The only taxes levied in this colony of 10,000 inhabitants are import duties and stamp taxes; no income tax, corporation income tax, net wealth or net worth tax, turnover tax or death duties exist. As exchange control is very liberal and the organisation of a Caymanian company a relatively easy matter, the Cayman Islands seem to be a fiscal "El Dorado", which in fact they are. The problems arise not in the Cayman Islands, but in the foreign countries the residents of which wish to enter into a fiscal relationship with the Cayman Islands.

In regard to the United States, for example, it would be desirable to avoid the Caymanian company being considered either a controlled foreign corporation or a personal/foreign personal holding company, since otherwise its profits would be subject to U.S. taxes. Various requirements as to ownership and type of income received must be complied with. The Caymanian company must have a bona fide business purpose, not be set up for tax avoidance only.

An additional U.S. tax problem may be the interest equalization tax, imposed on U.S. persons investing abroad. In this regard it should be noted that for purposes of the interest equalization tax the Cayman Islands are considered a "less developed country", so that U.S. persons may invest in its enterprises free of tax. The Bahamas and Bermuda, also tax havens, are no longer considered "less developed countries" for interest equalization tax purposes; investments therein are therefore subject to tax.

Non U.S. persons investing in Cayman Islands have similar obstacles to overcome in order to obtain the full benefit of Caymanian tax facilities. Although the problem may be different, persons residing in other well developed countries have to avoid the numerous pitfalls which form a part of their national tax systems.

An overall view of the Cayman Islands as a new base for foreign companies and trusts, written by Marshall J. Langer and W.S. Walker[1], has been published in the series Tax Ideas—Transaction Tax Guide, Prentice Hall, Englewood Cliffs, New Jersey, U.S.A. We recommend it as an introduction to the possibilities of the Cayman Islands for investors seeking a suitable place for the establishment of a company carrying on international operations. While numerous problems resulting from the tax laws of the countries of residence are pointed out therein, it would seem that with advise from a domestic tax advisor competent in this area these and any others inherent could be overcome.

DR. J.C.L. HUISKAMP

1 Library of the International Bureau of Fiscal Documentation, no. L 1322.

ARTICLES

SIDNEY I. ROBERTS:

THE FORCE OF ATTRACTION DOCTRINE IN THE UNITED STATES TAX LAW TODAY

CONTENTS:

I. FORCE OF ATTRACTION UNDER THE CODE
- A. Prior Law
- B. The Foreign Investors Tax Act
  - 1. Change in Activities of a Foreign Taxpayer
  - 2. Income From Real Property

II. FORCE OF ATTRACTION UNDER THE TREATIES
- A. United States Treaties Adopting the Force of Attraction Principle
- B. Exceptions to the Force of Attraction Principle

III. IMPACT ON TREATIES OF THE FOREIGN INVESTORS TAX ACT
- A. Section 894(b): Unilateral Treaty Revision
- B. Business Income (Industrial and Commercial Profits)

The Foreign Investors Tax Act of 1966[1] introduced several changes into the United States regime of taxation for foreign persons. One of these changes reflects a fundamental change in the rationale of prior law: the "abandonment" of the force of attraction principle.

I. FORCE OF ATTRACTION UNDER THE CODE

A. Prior Law

Prior to enactment of the Foreign Investors Tax Act, the Internal Revenue Code applied the "force of attraction" principle in the regime of income taxation for foreign persons. Under this principle, if a foreign taxpayer was engaged in trade or business in the United States, all of the taxpayer's income from United States sources was "attracted" to the United States trade or business without regard to the actual relationship of the income to the United States business, thereby subjecting all such income to United States taxation at the regular rates applied to taxable income. Thus, if a nonresident alien individual was engaged in trade or business in the United States at any time during the taxable year, he was subject to United States tax at the regular rates on all of his taxable "nonbusiness" income from United States sources, whether or not such income was in fact connected with the trade or business carried on in the United States. For example:

(1) Suppose a foreign taxpayer engaged in trade or business in the United States received dividends and interest from domestic corporations on investments which were

1 Title I, Public Law 89-809, 80 Stat. 1539 (1966) (hereinafter cited "Foreign Investors Tax Act").

made by the home office of the foreign taxpayer abroad and which were entirely unrelated to the taxpayer's trade or business in the United States. Had the foreign taxpayer not been engaged in trade or business in the United States, that income would have been subject to tax at the flat 30% rate applied to gross income. However, since the taxpayer was engaged in trade or business in the United States, under the Code prior to the Foreign Investors Tax Act, he was subject to tax on that income at the regular rates applied to taxable income.

(2) Suppose a foreign taxpayer engaged in trade or business in the United States derived income from sources within the United States from a casual sale of goods in the United States, the activities involved in such sale being entirely unrelated to the activities which constituted a trade or business in the United States, and the goods being of a different kind than those involved in the taxpayer's United States business. These sales would not have been subject to United States tax if such sales constituted the only activities of the foreign taxpayer in the United States. However, since the taxpayer was engaged in trade or business in the United States, prior to the Foreign Investors Tax Act, the foreign taxpayer was subject to tax at the regular rates applied to his entire taxable income, including his income from this sale. Thus, the application of the force of attraction principle under the Code prior to the Foreign Investors Tax Act may be summarized as follows: Because the taxpayer was engaged in trade or business in the United States, he was subjected to United States tax at regular rates applied to taxable income including (1) nonbusiness income that would otherwise have been taxed at the flat 30% rate applied to gross income and (2) business income that would otherwise have been exempt from United States tax. Thus, the force of attraction principle focuses on a foreign taxpayer engaged in trade or business in the United States.

B. The Foreign Investors Tax Act

The primary reasons given for dissatisfaction with the pattern of taxation under prior law was that it operated to deter foreign taxpayers engaged in a United States business from investing in the United States, as well as to inhibit foreigners already investing in the United States from commencing any United States business activities.[2] Furthermore, the adverse results could be avoided by undertaking the two classes of activities through separate corporate entities.[3] Accordingly, to encourage foreign investment in the United States,[4] the Foreign Investors Tax Act amended the Code to abandon the "force of attraction" principle insofar as it applies to "nonbusiness" income, but not as it applies to "business income."[5] Thus, as a general rule, §871, and §§ 881 and 882 of

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2 Report to the President of the United States from the Task Force on Promoting Increased Foreign Investment in United States Corporate Securities and Increased Foreign Financing For United States Corporations Operating Abroad 27 (1964).

3 Surrey, The United States Tax System and International Tax Relationships, XVII Tax Executive 104, 110 (1965).

4. H. Rep. No. 1450, 89th Cong., 2d Sess. 6, 14-15 (1966); S. Rep. No. 1707, 89th Cong., 2d Sess. 9 (1966).

5 The terms "business income" and "nonbusiness income" are not statutory words of art but merely shorthand expressions: Business income refers to income which is ordinarily related to a trade or business conducted in the United States and is subject to tax at the regular rates applied to taxable income, and nonbusiness income refers to income which is ordinarily unrelated to a trade or business carried on in the United States and is subject to tax at the flat rate of 30% applied to gross income.

the Code, which prescribe the regime of taxation for nonresident alien individuals and for foreign corporations, respectively, no longer provide rules for "nonbusiness" income which differ depending merely on whether or not the foreign taxpayer is engaged in trade or business in the United States. Instead, in the case of a foreign taxpayer engaged in trade or business in the United States, the distinction is drawn on the basis of whether the "nonbusiness" income is or is not effectively connected with the taxpayer's United States business. A foreign taxpayer engaged in trade or business in the United States is taxed at the regular rates applied to taxable income effectively connected with the conduct of a trade or business within the United States and at the 30% rate applied to gross income not effectively connected with the conduct of that business. Parenthetically, it may be noted that the abandonment of the force of attraction principle was not motivated entirely by a desire to lighten the tax burden of foreign taxpayers. Under prior law, as now, a foreign corporation not engaged in trade or business in the United States was taxed at 30% on United States dividends received, with no allowance of the 85% dividends received deduction.[6] Under prior law, it could gain the advantage of the dividends received deduction by engaging in an entirely unrelated trade or business in the United States. Under the Foreign Investors Tax Act, the dividends received deduction is available only if the dividends are effectively connected with the conduct of the United States trade or business.[7]

Unhappily for those who cherish tax simplicity, the distinction between "business" and "nonbusiness" income is merely an oversimplification of the applicable Code provisions. To be more precise and yet retain some succinctness of expression, we must devise a term, "Class A income", a term not used either in the Code, the Regulations or the legislative history. "Class A income" is used herein to refer to income described in §871(a)(1), applicable to nonresident alien individuals, and §881(a), applicable to foreign corporations, without regard to whether such income is or is not effectively connected with the conduct of a United States business. Thus, Class A income includes only income from United States sources and only income of the following classes:

(1) Interest, dividends, rents, compensation and other fixed or determinable annual or periodical income (a classification of income found in prior law).

(2) Gains described in §631(b) and (c), relating to timber, coal and iron ore.

(3) In the case of nonresident aliens but not foreign corporations: gains described in §§402(a) (2) and 403(a) (2), relating to distributions from employee trusts and employee annuity plans.

(4) In the case of nonresident aliens but not foreign corporations: gains on transfers described in §1235, relating to transfer of patents made on or before October 4, 1966.

(5) In the case of obligations issued after September 28, 1965, amounts which, under §1232 (relating to obligations of a corporation issued at a discount), are treated as gains from the sale or exchange of noncapital assets.

(6) Gains from the sale after October 4, 1966, of patents, copyrights, secret processes, good will, trademarks, trade brands, franchises, or other like property (a) to the extent that such gains are from payments which are contingent on productivity, use or disposition, or (b), if more than 50% of the gain in any taxable year is from payments which are so contingent, then all of the gain.

6 I.R.C. § 243.
7 I.R.C. § 882(c)(1)(A).

With this definition, it may be said with more precision that the Foreign Investors Tax Act abandoned the force of attraction principle in the regime of taxation for foreign taxpayers in this respect: A foreign taxpayer engaged in trade of business in the United States is taxed at the 30% rate applied to gross income on "Class A income" (i.e., the classes of income described in §871 (a)(1) and 881(a)) and, in the case of a nonresident alien individual present in the United States for 183 days or more, on capital gains, provided such income is not effectively connected with the conduct of a United States business. In the case of nonresident alien individuals present in the United States for less than 183 days and foreign corporations, capital gains not included in Class A income are excepted from tax if the gains are not effectively connected with the conduct of a trade or business within the United States.

The force of attraction principle persists, however, under the Code in the case of a taxpayer engaged in trade or business in the United States: income other than Class A income and capital gains is treated as effectively connected with the conduct of a United States business, even though such income has in fact no connection (i.e., under the criteria described in §864(c)(2)) with the conduct of a trade or business in the United States.[8] A few situations may illustrate some of the oddities that may arise from the vestiges of the force of attraction principle:

(1) A nonresident alien individual engaged in trade or business in the United States by virtue of his rendering personal services therein, makes a casual sale of inventory, title passing in the United States. Although the income from the sale has in fact no relationship to the business of rendering personal services, the income from the sale is classified as income effectively connected with the conduct of a United States business. If the alien had not been engaged in the business of rendering services, the income from the casual sale would have been entirely exempt.

(2) A nonresident alien author performs personal services within the United States for a United States corporation engaged in the production of a motion picture. In the same taxable year he sells in the United States, for a lump sum, a manuscript entirely unrelated to the personal services he renders. He is subject to tax on his gain from the sale of the book at regular (graduated) rates. Since the income from the sale is neither Class A income nor capital gain,[9] it is classified as effectively connected with the conduct of his United States business. If he had not been engaged in trade or business in the United States during the taxable year, the gain would have been exempt from tax.

(3) A foreign corporation engaged in trade or business in the United States in the manufacture and sale of widgets is subject to tax on gain from the sale of stock within the United States, even though stock is held for investment and is entirely unrelated to the widget business, if the gain from such stock is not a capital gain, for example, under the "collapsible corporation"[10] or "foreign investment company"[11] provisions of the Code. If the foreign corporation had not been engaged in the widget business in the United States, the gain would have been exempt from tax. The result, for example, in the case of gain not qualifying as capital gain under the collapsible corporation provisions, is merely to increase the penalty for the unwary taxpayer. Instead of merely

8 I.R.C. § 864(c)(3).
9 I.R.C. § 1221(3).
10 I.R.C. § 341.
11 I.R.C. § 1246.

(sic) paying tax at ordinary income tax rates rather than at the capital gains tax rate, as in the case of domestic corporation, the foreign corporation pays tax at ordinary income tax rates, which in many cases could have readily been avoided: by segregating in a separate entity the United States business activities or by selling the stock outside the United States.

1. Change in Activities of a Foreign Taxpayer.—As indicated in the discussion of the previous illustrations, the force of attraction principle applies only to a foreign taxpayer engaged in trade or business in the United States during the taxable year. A foreign corporation not engaged in a trade or business within the United States or a nonresident alien present in the United States for less than 183 days not so engaged is subject to tax only on Class A income; and a nonresident alien present in the United States for 183 days or more during the taxable year is subject to tax also on net capital gains.

The Code adopts the principle of fixing the status of a foreign taxpayer for an entire taxable year; Sections 871(b) and 882 impose tax at regular rates on foreign taxpayers "engaged in trade or business in the United States during the taxable year"[12] and §864(c)(1)(B) provides that in the case of a foreign taxpayer not engaged in trade or business "during the taxable year," no income shall be treated as effectively connected with the conduct of a United States business. Thus the non-resident alien author in the previous illustration who is engaged in trade or business in the United States in January, 1968, is taxed on the income from the manuscript sold in the United States in December 1968, but not if he sells it in January 1969, provided he is not engaged in trade or business in the United States at any time during the calendar year 1969. Similarly, if the foreign corporation previously referred to, reporting on a calendar year basis, discontinues the conduct of its United States widget business on June 30, 1968, it is taxable at regular rates on effectively connected income realized after June 30, 1968, but during the calendar year 1968, from it discontinued trade or business, as well as on, for example, gains realized after June 30, 1968, but during the calendar year 1968, from the sale of stock of a collapsible corporation, even though such income has no relationship to its discontinued business.

On the other hand, suppose that income is realized during the calendar year 1969 due to the taxpayer's business activity during the calendar year 1968, where the taxpayer is not engaged in trade or business in the United States at any time during the entire calendar year 1969. In such a case, the foreign taxpayer is subject to tax at the 30% rate applied to gross income realized in 1969 but only if the income constitutes income from United States sources and is either Class A income or, in the case of a nonresident alien present in the United States for at least 183 days, capital gains. Other income realized in 1969, including income from the widget business carried on in the United States in 1968, escapes tax. Thus if the foreign corporation discontinues its United States widget manufacturing business in December 1968, thereafter engages in no activities in the United States, and sells its idle machinery in 1969, it would seem that the gain on sale of the plant would escape United States tax.

This result obtains, however, only if the taxpayer is not engaged in any trade or business within the United States at any time during 1969. For example, if a foreign taxpayer discontinued in 1968 its widget business conducted in the United States but commenced therein a new trade or business

12 Emphasis added.

in 1969, income from United States sources realized in 1969 from its discontinued widget business would be taxed as effectively connected United States source income.[13] This result requires a close scrutiny of the statutory provisions, for example, the difference between the words "a" and "such" in the following provisions (emphasis added):

> I.R.C. §871(b)(1): "A nonresident alien individual engaged in trade or business within the United States during the taxable year shall be taxable as provided in section 1 or 1201(b) on his taxable income which is effectively connected with the conduct of a trade or business within the United States."
>
> I.R.C. §864(c)(2): "In determining whether an asset is used in or held for use in the conduct of such trade of business..."

An issue in which the result is not entirely clear is how the force of attraction principle applies to the discontinued business of a foreign taxpayer with an office or other fixed place of business in the United States who would have been subject to tax on foreign source income attributable to that fixed place of business. Suppose such a taxpayer is engaged in the active conduct of a licensing business in the United States through its United States fixed place of business and licenses patents to licensees outside the United States. In 1968, the taxpayer discontinues its business within the United States and abandons its fixed place of business. If it were not engaged in trade or business in the United States at any time during the calendar year 1969, royalty income realized in 1969 from patents licensed through its United States fixed place of business in 1968 would not be subject to tax. The difficult issue arises where in 1969 it engages in another trade or business in the United States without having a fixed place of business therein. Would it be taxable in 1969 on foreign source income realized in 1969 where such income was attributable to its discontinued fixed place of business? An argument in favor of taxability would be based on a literal reading of the Code: Since the foreign taxpayer is engaged in trade or business in the United States during the calendar year 1969, it is taxed on effectively connected income.[14] Section 864(c)(4) provides that foreign source income shall be treated as effectively connected income if the foreign taxpayer "has an office or other fixed place of business within the United States" to which such income is attributable, with no express requirement that it have such a fixed place of business during the taxable year. On the other hand, it may be argued that the tense of the verb in the quoted phrase and the emphasis elsewhere on the taxable year in classifying a foreign taxpayer,[15] require that it "has" a fixed place of business during the taxable year in which the income is realized. For similar reasons, it is not entirely clear whether income from foreign sources realized after the taxpayer discontinues his fixed place of business in the United States but in the same taxable year as the discontinuance, is treated as effectively connected; here the issue is whether the statute requires that the taxpayer "has" a fixed place of business at the time the income is realized. On balance it would appear that the argument in support of taxability in such a case is the more likely to prevail. Thus the foreign taxpayer would be subject to tax on foreign source income realized during the balance of 1968 subsequent to the discontinuance of its fixed place of business in

13 H.Rep. No. 1450, supra note 4, at 72.

14 I.R.C. §§ 871(b)(1), 882(a)(1).

15 E.g., §§ 871(b)(1), 882(a)(1) and 864(c)(1)(B).

the United States as well as during the entire calendar year 1969 where it is engaged in trade or business in the United States at any time during the calendar year 1969.

2. Income From Real Property.—In respect of one class of income which is taxed as effectively connected income under the Code, the force of attraction principle does not apply. Income from real property may or may not constitute a trade or business within the United States depending upon the extent of the activity of the foreign taxpayer in respect of the real estate.[16] If the income is not effectively connected with the conduct of a United States business, the rental income is fixed or determinable annual or periodical income subject to tax at 30% applied to gross income. In the case of such income not effectively connected with the conduct of a United States business, the Code, as amended by the Foreign Investors Tax Act, provides an election, described below. A similar election which differs in some important aspects is available in some of the treaties to which the United States is a party.

A foreign taxpayer who during the taxable year derives income from real property located in the United States, or from any interest in such real property, may elect to treat the income as "effectively connected with the conduct of a United States trade or business" and subject to tax at regular rates applied to taxable income, whether or not the taxpayer is engaged in trade or business within the United States during the taxable year.[17]

Income subject to the election includes: (1) gains from sale or exchange of such real property; (2) rents or royalties from mines, wells or other natural deposits; and (3) gains described in § 631(b) and (c), relating to certain timber, iron ore and coal royalties. The effect of the election is not to treat the electing taxpayer as engaged in trade or business in the United States but merely to "treat all such income" from real estate "as income which is effectively connected with the conduct of a trade or business within the United States" and to tax "such income" as provided in § 871(b)(1) or § 882(a)(1).[18] For example, an electing foreign taxpayer who made a casual sale of a noncapital asset in the United States but performed no other activities therein, would not appear to be subject to tax on the gain from the casual sale; if he were in fact engaged in trade or business in the United States, he would be subject to tax on that income since income other than Class A income and capital gains is always considered effectively connected with the conduct of a United States business. Thus, it may be said that the force of attraction principle has no application in respect of income from property not covered by the election to a taxpayer not in fact engaged in trade or business in the United States but merely by virtue of his election, taxed on income from real property in the same manner as one so engaged.

II. FORCE OF ATTRACTION UNDER THE TREATIES

While earlier United States treaties generally adopted the force of attraction principle, some provisions of the earlier treaties did not do so. Moreover, some of the more recent treaties, beginning with the 1965 German Protocol, expressly reject the force

16 See Roberts &Warren, U.S. Income Taxation of Foreign Corporations and Nonresident Aliens (March 1, 1966), V/3C.

17 I.R.C. §§ 871(d), 882(d).

18 I.R.C. §§ 871(d)(1), 882(d)(1) (Emphasis added).

of attraction principle. Before proceeding to discuss the impact of the Foreign Investors Tax Act, it may be useful to review briefly the provisions of the treaties prior to its enactment. The "force of attraction" principle under the treaties may be illustrated as follows:

(1) Suppose a foreign enterprise has a permanent establishment in the United States and also realizes industrial and commercial profits entirely unrelated to the permanent establishment, for example: a foreign enterprise has income from the sale of a line of goods entirely unrelated to the goods sold through the permanent establishment, and marketed in the United States directly from the home office abroad through an independent agent acting in the ordinary course of his business as such.

(2) Or suppose such an enterprise has dividend, interest or royalty income from investments made by the home office that are entirely unrelated to the permanent establishment in the United States.

The force of attraction issue may be stated thusly: Does the existence of the permanent establishment affect only the taxation of the industrial and commercial profits attributable to the permanent establishment, or does the permanent establishment "attract" the unrelated income not in fact attributable to the permanent establishment, with the result that the unrelated income, as well as the income attributable to the permanent establishment, is denied the advantage of the treaty?

A. United States Treaties Adopting the Force of Attraction Principle

Under the treaties premised on the "force of attraction" principle, the permanent establishment in the United States "attracts" all business and investment income, even though unrelated to the permanent establishment, thereby denying the treaty benefits to such unrelated income and subjecting it to the regular rates of tax required under the Code.[19] Thus, under the force of attraction principle, where a foreign enterprise has a permanent establishment in the United States, all industrial and commercial profits derived from United States sources, even though not attributable[20] to the permanent establishment (for example, income from goods marketed directly from the home office abroad through an independent agent in the United States) are subject to United States tax.[21] Similarly, such a foreign enterprise is generally denied the exemption or reduced rate of tax on capital gains, dividends, interest and royalties, etc., from United States sources even though such income is entirely unrelated to the permanent establishment, for example, in the case of unrelated investment portfolios held and controlled from the home office abroad.

B. Exceptions to the Force of Attraction Principle

The Modifying Protocol signed with the Federal Republic of Germany in 1965, prior to enactment of the Foreign Investors Tax Act, represented a shift in the United States policy away from the force of attraction principle.

Under the German Protocol if the German enterprise is engaged in trade or business in the United States through a permanent establishment, it is taxable on industrial and commercial profits which are attributable to

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19 See Surrey, supra note 3, at 109-10.

20 See The Organization for Economic Cooperation and Development Draft Convention For The Avoidance of Double Taxation With Respect To Taxes On Income And Capital, Art. 7(2).

21 See, e.g., Reg. § 504.105(c)(2) (Belgium); Reg. § 519.104(c) (Canada).

the permanent establishment. However, unlike the OECD Draft Convention, which taxes income only to the extent that it is attributable to the permanent establishment,[22] the German Protocol further provides that a German enterprise having a permanent establishment in the United States is also taxable on any industrial and commercial profits derived from United States sources from sales of goods or merchandise of the same kind as those sold by the permanent establishment or from business transactions of the same kinds as those effected through the permanent establishment.[23] Thus, to this extent the force of attraction principle persists in the German Protocol.

Like the 1965 German Protocol, the 1966 United Kingdom Supplementary Protocol reflects a shift away from the force of attraction principle: a United Kingdom enterprise engaged in trade or business in the United States is subject to United States tax only on the industrial and commercial profits which are "directly or indirectly attributable to the permanent establishment."[24] It is not clear, however, whether the quoted language would yield different results here than under the German Protocol; whether, for example, income from the sale of goods "of the same kind as those sold" through the permanent establishment[25] would be considered "indirectly attributable" to the permanent establishment.[26]

Similarly, with respect to income other than industrial and commercial profits, the 1965 German Protocol also abandons the force of attraction principle. Thus, the tax advantages accorded by the treaty to dividends,[27] interest,[28] royalties,[29] and capital gains[30] are available in the case of income from assets not "effectively connected" with a permanent establishment. The Memorandum of Understanding[31] which supplements the Protocol, provides guidelines for construing this elusive term. The guidelines prescribed under the German Protocol for determining whether nonbusiness income is effectively connected with a permanent establishment are not stated in precisely the same way as the guidelines prescribed under the Code for determining whether income from United States sources is effectively connected with the conduct of a trade or business in the United States.[32] Nevertheless, it may be anticipated that the future development of the law will reflect a tendency to accord a similar interpretation to the concept under the treaties and under the Code.

United States treaties signed after the 1965 German Protocol similarly reflect the United States shift away from the force of attraction principle with respect to nonbusiness income. For example, the exemption accorded to royalties under the United Kingdom treaty is denied if the foreign entity has a permanent establishment but only if the "right or property giving rise to the royalties is effectively connected with such permanent establishment";[33] and a similar limitation is applied in the treaty provisions exempting

22 Art. 7(1) and (2). See OECD Commentary, paras. 6–9, 1963 OECD Report 80–82.
23 Germany, Art. III(1) (Prot. Art. 3) (last sentence).
24 United Kingdom, Art. III(1) Prot. Art. 3).
25 Germany, Art. III(1).
26 United Kingdom, Art. III(1).
27 Germany, Art. VI(7) (Prot. Art. 4).
28 Germany, Art VII(3) (Prot. Art. 5).
29 Germany, Art. VIII(4) (Prot. Art. 6).
30 Germany, Art. IXA(3) (Prot. Art. 8).
31 Hearings on S. Exec. Docs. G, I, Before a Subcommittee of the Senate Committee on Foreign Relations, 89th Cong., 1st Sess. 25, para. 3 (1965).
32 I.R.C. § 864(c)(2).
33 Art VIII(3). Similarly, Netherlands, Art. IX (3).

interest[34] and capital gains[35] and reducing the rate on dividends.[36]

While the 1965 German Protocol is the first treaty in which the United States generally abandons the force of attraction principle, a few of the earlier treaties provided limited exceptions for unrelated investment income. In the Swedish treaty, the exemption from United States tax of royalties paid, for example, to a nonresident alien who is a resident of Sweden, is not conditioned upon the absence of a permanent establishment.[37] Moreover, the Japanese Protocol of 1962 modified the force of attraction doctrine by extending the treaty benefits accorded to dividends, interest and royalties to Japanese recipients who had a permanent establishment in the United States by reason of a construction project installation, or assembly project of more than 12 months duration;[38] however, the dividends, interest or royalties must be such as are not attributable either to the trade business or assets of the permanent establishment or to a transaction which is of a kind normally engaged in by such permanent establishment.[39]

Finally, certain provisions granting tax advantages have traditionally not adopted the force of attraction principle, for example, the exemption accorded in some treaties[40] to dividends paid by a foreign corporation to foreign persons, and the exemptions for commercial travelers,[41] private pensions and annuities, and students and teachers.

III. IMPACT ON TREATIES OF THE FOREIGN INVESTORS TAX ACT

A. Section 894(6): Unilateral Treaty Revision

As previously indicated, the earlier treaties generally adopted the "force of attraction" principle, both in respect of industrial and commercial profits and other income as well. On the other hand, the thrust of the amendments to the Internal Revenue Code made by the Foreign Investors Tax Act is to tax alike all foreign taxpayers, whether or not engaged in trade or business in United States on income which is not effectively connected with the conduct of a trade or business in the United States. To achieve a consistent pattern under the treaties, the Act added § 894(b) to the Code:

> "(b)PERMANENT ESTABLISHMENT IN UNITED STATES.—For purposes of applying any exemption from, or reduction of, any tax provided by any treaty to which the United States is a party with respect to income which is not effectively connected with the conduct of a trade or business within the United States, a nonresident alien individual or a foreign corporation shall be deemed not to have a permanent establishment in the United States at any time during the taxable year."[42]

With respect to incomeother than industrial and commercial profits, the Belgian treaty is typical:

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34 Art. VII(3). Similarly, Netherlands, Art. VIII(2).

35 Art. XIV(3). Similarly, Netherlands, Art. XI(2).

36 Art. VI(4). Similarly, Netherlands, Art. VII(3).

37 Art. VI. See Rev. Rul. 60-288, 1960-2 Cum. Bull. 265, 266 n.14. But see Reg. § 520.109(a) (Sweden).

38 See Art. II(1)(c) (third sentence).

39 Art. VI(1)(b) (interest); Art. VIA(2)(b) (dividends); Art. VII(1)(b) (royalties). See S. Exec. Rep. No. 10, 88th Cong., 2d Sess. 68, 81 (1964).

40 Compare Netherlands, Art. XII, with Switzerland, Art. XIV(1).

41 But see United Arab Republic, Art. VIII(1)(b).

41(a). S. Rep. No. 1707, supra note 4, at 40.

42 This provision is inapplicable to expatriates whose tax is computed under I.R.C. § 877(b).

"The rate of United States tax on dividends derived from sources within the United States by a resident or corporation or other entity of Belgium not having a permanent establishment within the United States shall not exceed 15 percent."[43]

Similarly, a Belgian entity having a permanent establishment in the United States is expressly denied the reduced (15%) rate accorded by the treaty for interest[44] and the exemption accorded to royalties.[45] These provisions must now be read in light of § 894(b), of the Code; under this provision the reduced rate accorded to dividends and interest and the exemption for royalties is available to a Belgian entity despite its permanent establishment in the United States, provided the income is not effectively connected with the conduct of a business carried on in the United States.

A few early treaties expressly defer to internal tax law, to determine whether the force of attraction principle shall apply to nonbusiness income. For example, the Swiss treaty provides that the term "industrial and commercial profits" does not include dividends, interest, rents or royalties, or remuneration for personal services, but states: "such excepted items of income shall, subject to the provisions of this Convention, be taxed separately or together with industrial or commercial profits in accordance with the laws of the contracting states."[46] Under the Treasury Regulations issued pursuant to prior law, dividends (for example) of a Swiss entity having a permanent establishment in the United States were subject to tax at regular rates along with the industrial and commercial profits allocable to the permanent establishment, even though the dividends had no connection with the permanent establishment.[47] As a result of the Foreign Investors Tax Act, if such dividends are not effectively connected with the conduct of a United States business, they are currently subjected to tax at the 15% rate accorded by the treaty.[48]

B. Business Income (Industrial and Commercial Profits)

In respect of industrial and commercial profits, the earlier treaties also expressly adopt the force of attraction principle. For example, the Australian treaty provides:

"If it [the Australian enterprise] . . . is so engaged [in trade or business in the United States through a permanent establishment in the United States], United States tax may be imposed upon the entire income of that enterprise from sources within the United States."[49]

Consider the case previously given: goods are marketed in the. United States, title passing therein, through an independent agent in the United States, entirely separate from its permanent establishment in the United States. Since the Australian enterprise is engaged in trade or business through a permanent establishment in the United States, the treaty does not bar the United States taxation of the goods marketed through the independent agent.

Nor does the Code yield a contrary result:

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43 Art. VIII(1). Accord, e.g., Switzerland, Art. VI(1) (15% rate); Trinidad and Tobago, Art. 3(2) (25% rate).

44 Art. VIIIA. Accord, e.g., Switzerland, Art. VII(1) (5% rate); Luxembourg, Art. VIII exemption).

45 Art. IX(2). Accord, e.g., Luxembourg, Art. VII (exemption); Switzerland, Art. VIII (exemption).

46 Switzerland, Art. II(1)(h). Accord, Union of South Africa, Art. V(3).

47 Reg. §§ 509.105(c); 509.108(a).

48 Art. VI(1).

49 Australia, Art. III(1). Accord, Austria, Art. III(1); Art. III(1)(a).

Section 894(b) is applicable only to income not effectively connected with the conduct of a trade or business in the United States.[50] And under the Code, income from the sale of such goods is treated as effectively connected with the conduct of a United States business.[51] Thus, the force of attraction principle remains applicable under these treaties in respect of the income from the sales through the independent agent.

The language of other treaties raises a further problem. For example, the Belgian treaty provides:

> "An enterprise [of Belgium] . . . is not subject to taxation by [the United States] . . . in respect of its industrial and commercial profits except in respect of such profits allocable to its permanent establishment in [the United States] . . ."[52]

The regulations under these treaties, promulgated prior to enactment of the Foreign Investors Tax Act of 1966, provide that all industrial and commercial profits of the enterprise from sources within the United States shall be deemed to be allocable to the permanent establishment and are therefore subject to United States tax, whether or not such sales were actually made by the permanent establishment.[53] Thus, these regulations generally provide that industrial and commercial profits from United States sources are allocable to the permanent establishment even where the sale is made by a bona fide commission agent acting in the ordinary course of his business as such. Accordingly, the Treasury's position in these regulations is that despite the language in a particular treaty, the presence of a permanent establishment will result in the taxation of all industrial and commercial profits from United States sources, whether or not in fact attributable to the permanent establishment. This position seems to interpret the phrase "allocable to its permanent establishment", presumably by reference to the then applicable internal tax law of the United States,[54] to mean industrial and commercial profits from sources within the United States. This would seem to be a strained construction of the phrase, especially since other provisions of the treaty use the phrase "from sources within the United States."[55] Moreover, it may be questioned whether in the context

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50 See p. 22 supra.

51 I.R.C. § 864(c)(3).

52 Belgium, Art. III(1). Accord, Canada, Art. I; Sweden, Art. II;
Union of South Africa, Art. V(1);
France, Art. 3.

53 Reg. § 504.105(c)(2) (Belgium); Reg. § 519.104(c) (Canada); Reg. § 514.105(c) (France); Reg. § 520.104(c) (Sweden). While regulations have not been issued under the treaty with the Union of South Africa, the Report of the Acting Secretary of State, April, 23, 1947, S. Exec. Doc. O, 80th Cong., 1st Sess. 3 (1947), 2 U.S. Tax Conv. 2463, 2465, is consistent with the regulations cited above.

54 In the Luxembourg treaty, the position taken in the regulations is more clearly stated: Article III(1) contains the provision of the OECD Draft Convention, that the contracting States will tax only the industrial and commercial profits of an enterprise which are attributable to the permanent establishment. However, a final sentence, not found in the Draft Convention, has been added: "In applying the preceding sentence for purposes of the United States tax, all industrial or commercial profits of the enterprise from sources within the United States shall be deemed to be attributable to the permanent establishment."

55 E.g., Belgium, Art. VIII; France, Art. 6A. See Norr, The Swedish-American Tax Treaty Revised, 33 Geo.Wash. L. Rev. 467, 488 n. 108 (1964). Cf. Germany, Art. III(1) (second sentence) (differentiating between profits "attributable to" the permanent establishment and profits "derived from sources within" the United States from sales of merchandise or from business transactions of the same kind as those effected through the permanent establishment).

of the term "allocable to its permanent establishment," it may properly be interpreted by reference to the internal law. Such reference to the internal tax law is particularly difficult in respect of United States source income because (a) the internal tax law of the United States does not expressly refer to income allocable to a permanent establishment but to income effectively connected with the conduct of a trade or business within the United States,[56] and (b) the internal tax law does refer to income "allocable" to an office or other fixed place of business in the United States,[57] but only in respect of income from sources without the United States. Moreover, it may be argued that the term "allocable to" a permanent establishment should be interpreted by reference to a common provision found, for example, in the Belgian treaty,[58] which provides that there shall be "attributed to" the permanent establishment the profits it would derive if it were an independent enterprise. Accordingly, it is not entirely clear whether under the Belgian treaty income from sources within the United States which is entirely unrelated to the permanent establishment in the United States should be treated as "allocable to" the permanent establishment. If the term "allocable to its permanent establishment" is not to be determined by reference to the internal tax law of the United States, then industrial and commercial profits in fact not connected with the permanent establishment are not subject to tax under the treaty. On the other hand, if, as implied by the prior regulations, the term is interpreted by reference to the internal tax law of the United States, another issue arises: whether the reference is to the internal law in effect at the time of negotiation of the treaty or under the internal law currently in effect. If the term "allocable to its permanent establishment" is interpreted, by reference to the internal tax law of the United States as in existence at the time of negotiation of the treaty, to mean: "from sources within the United States," the result would be the same as under the Australian treaty, discussed above. Moreover, even if the term is interpreted by reference to the internal tax law of the United States currently in effect, the result would also appear to be the same as under the Australian treaty, provided it can be found that the term „allocable to its permanent establishment" is governed by the rules of the Code which provide when income is treated as "effectively connected with the conduct of a trade or business within the United States."[59]

In one respect the force of attraction principle applies differently under the Internal Revenue Code, as well as under the earlier treaties as modified by § 894(b) of the Code, than it does under the recent treaties which expressly reject the force of attraction principle. This results because the Code applies the force of attraction principle with respect to "income" effectively connected with "the conduct of a trade or business within the United States";[60] whereas the treaties refer to income yielding assets which are effectively connected with a permanent establishment in the United States.[61] This distinction becomes important where a foreign taxpayer is engaged in two separate trades or businesses in the United States, only one of which is carried on through a permanent establishment therein.

Consider, for example, the case of a non-

56 I.R.C. § 864(c)(2).
57 I.R.C. § 864(c)(5).
58 Art. IV(1).

59 I.R.C. §§ 871(b)(1), 882(a)(1).
60 I.R.C. §§ 894(b), 864(c)(3).
61 E.g., United Kingdom, Arts. VI(4), VII(3), VIII(3).

resident alien individual engaged in trade or business in the United States through traveling salesmen not having the power to conclude contracts in the name of the nonresident alien, requisite to constituting a permanent establishment. Suppose further that the alien owns stock of a United States corporation acquired to manufacture goods which constitute the source of supply for the business carried on through the traveling salesmen; and that the nonresident alien also carries on an entirely separate trade or business through a permanent establishment in the United States. Under the earlier United States treaties, the reduced rate accorded to dividends would be expressly denied because the foreign taxpayer has a permanent establishment in the United States; moreover, § 894 (b) would not change the result, since the dividends are effectively connected with the conduct of a United States business, albeit not with a permanent establishment. On the other hand, under the United Kingdom treaty, for example, the dividends would be entitled to the 15% tax rate, since the holding of the stock is not effectively connected with a permanent establishment in the United States.[62]

62 Art. VI(4).

ADOLFO ATCHABAHIAN:

ALLOCATION OF THE TAXING POWER IN ARGENTINA BETWEEN THE CENTRAL GOVERNMENT AND THE PROVINCES

1. FOREWORD
2. CONSTITUTIONAL THEORY AND PRACTICE
3. SYSTEMS OF REVENUE APPORTIONMENT:
   I. Statutes in effect:
      A. *Internal taxes on consumption (excise taxes);*
      B. *Income capital gains, and sales taxes;*
      C. *Tax substitute on inheritance tax.*
   II. Proposals in the National Development Plan 1965-1969
4. CRITICISM AND CONCLUSIONS.
BIBLIOGRAPHY

1. FOREWORD

The main purpose of this article is to show how the federal system is performing in Argentina in the field of taxation.

Although the National Constitution defines quite clearly the spheres of competence which belong to each level of government, it does not determine specifically—with respect to the taxing power—what kind of taxes can be levied by the central government[1], on the one hand, and by the provinces, on the other[2].

In order to understand the problem more clearly, it is best to treat it taking for granted a divison into direct and indirect taxes.

As long as the chief, almost exclusive, source of revenue of the Argentine Republic were customs duties, no problem of allocation the taxing power between the central government and the states existed. But since the great depression of 1890, customs duties have not yielded enough revenue to the central government, and the government, seeking immediate financial resources, approved "internal taxes" on certain consumer goods, thus prompting discussions on the constitutional authority for doing so. Furthermore, new constitutional questions arose due to the establishment of the income tax in 1932, and later, other direct taxes, such as the excess profit tax in 1944, and the so-called "eventual profits tax" (impuesto a las ganancias eventuales), a sort of a tax on capital gains, in 1946, in order to tax income categories other than those included within the scope of the former income tax.

Thus, we shall examine the constitutional principles, and their evolution, from the legislative and judicial points of view, that is to say, how the Congress and the Supreme

1 Following Felix Morley ("Freedom and Federalism", Chicago, 1959, page 18), we say "central" government, not "federal" government, in the sense that in the federal system we must regard a government as a part, in other words, as a link of the chain in the federalism as a whole.

2 We will use "province", as well as "state", but in the Argentinian constitutional and political vocabulary, the former is used more often.

Court put in action the provisions of the Constitution.

2. CONSTITUTIONAL THEORY AND PRACTICE

Generally speaking, under the Constitution, we have to take for granted—as we said before—the division between direct and indirect taxes.

Then, bearing in mind what the Constitution states (3), and what arises from the jurisprudence of the Supreme Court of the Argentine Republic (4), the conclusions are (5):

I. To the central government belong:

a) customs duties, exclusively;

b) other indirect taxes in general, concurrently with the provinces;

c) direct taxes in exceptional circumstances, if it is necessary because of "defense, common security and general welfare", but only temporarily, and in a manner proportionally equal all over the country.

II. To the provinces belong:

a) indirect taxes in general, concurrently with the central government;

b) direct taxes in general, subject to the exceptional situations mentioned above (I.c.)

However, in spite of these constitutional provisions, the tax legislation in reality works in quite a different way.

Thus, the most important direct tax, both from the theoretical point of view and because of its yield, is levied by the central government. We are referring to the income tax, but the same can be said about other direct taxes.

The constitutional requirement that the direct taxes must be temporary—if they are established by the central government—, is fulfilled by a statement of limited duration of the effect of the statute and subsequent successive postponement of the expiration of the tax. This is the case with following major taxes: income tax, "eventual profits tax", the socalled "tax substitutive of inheritance tax", (and until it was abrogated, by the statute No 16.656, enacted in December 30th., 1964, the excess profit tax). The amounts yielded by them are distributed between the central and provincial governments[6]. Another, very important tax included in this legislation—as we shall see—, in spite of the fact that it is indirect, is the sales tax.

On the other hand, the internal indirect taxes—most of them on consumption—are collected by the central government. The provinces have given up their powers in this respect. The yield from this source is distributed between the central government and the provinces, according to the so-called "regime on the unification of internal taxes", which procedure is different from the way

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3 Articles 4, 9, 17, 67 (paragraphs 1 and 2), 104. See the comments by L.S. Rowe in "The federal System of the Argentine Republic" (Washington, 1921), specifically chapters V and VI.

4 See Santos P. Amadeo, "Argentine Constitutional Law", New York, Columbia University Press, 1943, pages 129/132; and more up-to-date "Poderes impositivos federaly provincial sobre los instrumentos de gobierno" (Buenos Aires, Guillermo Kraft Ltda., 1943, pages 45/52, by Carlos A. Adrogue.

5 See Horacio A. Garcia Belsunce, "Autonomia de los gobiernos locales en materia tributaria. La distribucion de los poderes impositivos", in the Volume "Jornadas de Derecho Tributario", edited by Montevideo. Universidad. Facultad de Derecho y Ciencias Sociales, pages 468-470.

6 Besides, we can mention two other taxes included in the same system, which nowadays have lost their importance: a tax on fiscally non justified increase of net worth and a tax on revaluation of assets. Finally, we must add the emergency tax, introduced in 1962 and still in effect: it represents a certain percentage—now, 15%—of the income tax liability, for individuals and corporations.

the yield from direct taxes is distributed.
The constitutional provisions are applied only with regard to customs duties, which are levied exclusively by the central government. But their significance nowadays is much less important than it was thirty years ago. However, it is necessary to say that since 1956 foreign trade has been a source of great revenue for the central government, by means other than customs duties; namely by a sort of charge on imports and withholding on exports, computed according to the exchange value of the goods imported or exported, respectively.
Direct taxes—inheritance tax, general property tax—different from those mentioned above, are levied by the states, within their own boundaries[7].
With regard to the states, the importance of the funds received by them from the different systems of apportionment in their revenue, depends upon the natural richness and economic development of each state. Thus, the so-called "poor provinces" are more dependent on the revenues received from the central government, by application of those systems.
Out of the twenty-two provinces which form the Argentine Republic, seven provinces which—from the population viewpoint—had almost 45 per cent of the total population of the country, in 1962 got more than half of their revenues from the taxes levied under their own tax systems[8]. On the other hand, the remaining fifteen provinces received 52 to 86 per cent of their revenues from the proceeds yielded by the central government and distributed thereafter.

3. SYSTEMS OF REVENUE APPORTIONMENT

1. Statutes in effect

A. *Internal taxes on consumption (excise taxes).*
The first internal taxes on consumption were enacted by the central government in 1891. Three products were reached by the statute: beer, matches, and playing cards. This created a very difficult problem of tax overlapping between the central government and the states. At the time, the states already had similar kind of taxes on consumption.
Very often the same taxes were levied on the same products by the two powers, a situation which was even more undesirable for the provinces.
This was the case even though according to the decisions of Supreme Court, both governmental spheres have taxing power in that respect[9]. But the difficulties that arose were, from the economic standpoint, very serious: sometimes there were taxes levied on taxes previously paid in other jurisdiction and included in the price of the products imposed.
After several attempts—by means of proposals presented before the Congress—for avoiding that overlapping, in 1935 a statute (No 12.139), was enacted about the so called "regime on unification of internal taxes", dealing with the taxes on consumption which are specified by the statute.

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7 The inheritance tax is also levied by the central government for the Federal District (Buenos Aires City), where the property tax is collected by the local authority, the Municipality of Buenos Aires City.
8 Each state has its own fiscal code, with the general rules of procedure, and the provisions governing each provincial tax; moreover, every year—according to such a code—a statute is enacted fixing the tax rates. The central government does not have a fiscal code; instead, the statutes are different for each tax, but there is a general statute relating to the procedure for the application and collection of national taxes.
9 See footnote 4.

At present the list of articles reached by those taxes is as follows: tobacco, alcohol, alcoholic beverages, lighters, insurance policies, combustibles and lubricator oils (there are also included in the system of apportionment additional taxes on gasoline and on lubricator oils), playing cards, wines, ciders and hydromels, matches, beers, dressing articles, luxurious objects, tires, sugar, spinning and silk textures, gaseous beverages, refreshments and sirups, extracts and concentrates. We must add that included in the same system of apportionment is the yield from the tax on purchasing and transference of automobiles.

The main goal of the above mentioned unifications was to concentrate in the central government the power to levy this kind of tax, and barring the states from enacting similar taxes within their jurisdictions.

The statute of 1935 was in effect for twenty years, and the feasibility of continuing it for ten years more was impeded due to the denouncement of the system by a state. Actually, under the statute, if any state did not denounce the system, the statute had a provision for automatic continuation for ten years. But in 1954, the Province of Corrientes claimed a change in the system, including the rates of distribution of the amount of taxes thus collected.

Therefore, the Congress studied a new regime and enacted, in 1954, the statute N° 14.390, to be effective for ten years from January 1st., 1955. It is still in effect with some modifications. Again, several provinces have denounced this system also—avoiding the implicit and tacit continuation of the statute for ten years—, but despite that fact it has been continued twice—for the years 1965 and 1966, respectively by the statutes N° 16.653 and 16.877, pending the end of special studies about the problem.

First of all, the statute requires the states to indicate their agreement with the system —by virtue of a legislative decision from the State Legislature—, in order to collect the amounts distributed, and bind themselves to abstain from the enactment of any taxes similar to those included in this system of distribution.

The participation in the amount of taxes collected, which belongs to the central government, on the one hand, and to the state governments, on the other, is determined in a manner directly proportional to the total population of the country and to the total population of the provinces in agreement with the system, respectively.

The portion which belongs to the provinces, is divided among them in the following way;

a) 98 per cent according to the population of each province, and according to its output of products taxed by these internal taxes on consumption, and its output of chief raw materials used in the manufacturing of those products. The proportions are:

	According to the population	According to the output
1955	84%	16%
1956	82%	18%
Since 1957	80%	20%

b) The remainder 2 per cent is distributed in inverse ratio to the amount which corresponds to each inhabitant in the population of the province, established according to the foregoing point a).

An Arbitral Tribunal created by the statute is entitled to decide whether or not a tax enacted by a province—or by a municipality or local authority thereof—is contrary to the unification regime. This Tribunal has the power to approve the distribution indices for each provincial government, taking into consideration the data mentioned at a) and b).

B. *Income, capital gains, and sales taxes*

A decree of January 19th., 1932, introduced the income tax by the central government[10]. At the beginning it was said—respecting the requirement stated in the Constitution (article 67, paragraph 2)—that it would be an "emergency tax", for three years, from January 1st. of the same year.

Article 38 of that decree referred to the distribution of the revenue, by the central government to the provinces, but nothing concrete was said in that respect, either in fixed amounts or in percentages.

Thereafter, by means of the budget for 1934 (statute n° 11.821, article 45), the Congress authorized the Executive Branch to make agreements with the provincial governments for the apportionment of income tax. The criterion for the agreements ought to take into account the population of each province, the respective income tax revenue, and the total amount of the revenue and the provincial public expenditures.

In the meantime, the central government had to advance certain amounts as part payments to the provinces. This means that they did not receive any amounts for the yields of 1932 and 1933.

According to another provision in the same article 45 in the statute N° 11.821, the provinces were bound to spend the advanced funds for the payment of teachers and employees salaries, public works, and other administrative expenses. This deserved a strong criticism, because it implied a limitation of the provinces' rights of spending the funds according to their own decisions.

We have said that the first Argentinian income tax was enacted for three years, from 1932 to 1934. But before its expiration, statute n° 12.147 extended it up to December 31st., 1944. Furthermore, more important for this survey, it introduced a percentage system for distributing the total proceeds of income tax between the central government, on the one hand, and the provinces and the Municipality of Buenos Aires City, on the other: the first would receive 82.5%; and the others, as a whole, the remaining 17.5% (11). This new method would be applied from January 1st., 1935, until December 31st., 1938.

Subsequently, other statutes continued that method: N° 12.578, for the year 1939; N° 12.599, for the year 1940; N° 12.679, for the year 1941; N° 12.778, for the year 1942; N° 12.816, for the year 1943. The decree 18.229, of December 31st., 1943(12), continued it for the years 1944 and 1945, as long as the decree 14.338 from May 20th., 1946, did the same for the year 1946 (12).

Since January 1st., 1947, until December 31st., 1955, statute N° 12.956 was in effect. This statute changed the system. It fixed new percentages, providing that those would be 79% for the central government, and 21% for the provinces and the Municipality of Buenos Aires City. A new kind of provision was that 2% of the latter would be distributed in inverse ratio to the population of Federal District (Buenos Aires City) and of the provinces.

On the other hand, by virtue of this statute the system was applied simultaneously to the

10 At that time there was a revolutionary government in power. That is the reason for the legal origin of the income tax: a decree. It was ratified by the Congress in the same year, after its introduction (statutes number 11.586 and 11.682). The latter is still the number used now, including each time the lastest amendments.

11 The same statute decided to regard as definitive the distribution already done for 1934.

12 This was a decree, not a law, due, again, to the fact that there was a revolutionary government.

revenue from the income tax, as well as the excess profit tax (existed since 1944), the tax on capital gains (enacted in 1946), and the sales tax (in effect since 1935)[13].

The decree 3.675, enacted on December 14th., 1955, continued the effect of the statute n° 12.956 during the year 1956, and in the meanwhile the decree 770[14], approved in 1957, did the same for the years 1957 and 1958.

Statute n° 14.788, enacted in 1958, contains the following apportionment method: it introduced a new system, determining higher percentages for the provinces in the years 1959 to 1963. Those percentages were, for the central government, 72% in 1959, decreasing 2% a year, down to 64% in 1963; and for the provinces 28% in 1959, increasing 2% a year, up to 36% in 1963.

Moreover, an important difference from the foregoing methods was that the Municipality of Buenos Aires City would receive its portion not along with the provinces, but from the central government's portion; the latter ought to give it 6% of the total proceeds from taxes included in the system.

Likewise, in 1962, the statute N° 16.450 (article 21), provided that from the portion belonging to the central government, 0.04% of the total proceeds from taxes included in the system, shall be allocated to the National Territory of "Tierra del Fuego, Antartida e Islas del Atlantico Sud"[15].

In 1963, statute N° 16.453 continued the effect of the statute n° 14.788 up to December 31st., 1964, but provided that the percentages would be 60% and 40%, instead of 64% and 36% for each part, according to the 1963's distribution.

Statute N° 16.653 did the same thing—it extended statute N° 14.788 with the amendments introduced by statute n° 16.453—, up to December 31st., 1965[16].

Statute N° 16.877 stated the continuation of this system till December 31st., 1966.

Finally, at present time, the statute N° 17.129 states a new apportionment, even though it maintains the system previously mentioned. The share belonging to each jurisdiction involved in that system, is as follows for the current year 1967:

1) 59,19% for the central government;
2) 35,46% for the provinces;
3) 5,32% for the Municipality of Buenos Aires City;
4) 0,03% for the National Territory of "Tierra del Fuego, Antartida e Islas del Atlántico Sud".

With respect to the rules which form the regime of apportionment, we can say that the portion belonging to the twenty two provinces is distributed among them in the following way:

1. 75 per cent:
   a. One third according to the population of each province, determined by the National Bureau of Statistics and Census, up to December 31st. of each basic year.
   b. One third according to the revenue collected for each province—excluding those provided for using the public credit, those given by the present system of apportionment under analysis, and the federal grants.

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13 This tax was established by statute number 12.143; its article 14 stated the same percentages of distribution as in the statute number 12.147, that is to say, 82,5% and 17.5%.

14 The reason for these decrees is the same as we cited in the footnotes 10 and 12.

15 These are the only parts of the Argentine Republic's territorry—aside from the Federal District, Buenos Aires City which do not have the status of a province.

16 We have to bear in mind that since January 1st., 1965, the excess profit tax has not been in effect, because it was repealed in 1964, by statute number 16.656.

c. One third according to the amount of expenditures of each province.

II. 25 per cent in equal parts among all the provinces.

The concept of the basis year arises from the following rules: the necessary indices, of distribution, in order to apply those provisions stated in the previous points I and II, are in effect for two years, and they are determined based on information concerning the last complete calendar year immediately preceding the date of the beginning of each two years period (the indices for 1959 and 1960 were an exception, because they were computed according to the data of 1959).

Pending the preparation of the final indices, the Treasury Department elaborated provisional ones, in order to permit the Argentine Nation's Bank to make payments to the provinces to the extent that the Bank—as a financial agency of the government—was receiving amounts of revenue included in the system.

The provinces get the right of participation in the distribution of revenue under the condition of their agreement to the system established by statute N° 14.788. It must be decided by means of a special provincial statute, which ought to state:

a. That the province accepts that system, without either limitations or reserves.
b. That the province assumes the obligation not to levy state taxes which are analogous to those included in this system of apportionment.
c. That the province assumes the obligation—during the period on which the system will be effective—to abrogate state taxes, and to promote the abrogation of local taxes, conflicting with the system.
d. That the province assumes the obligation for taking necessary decisions in order to get cooperation from the state and local agencies, with respect to gather data related to the gross national product and the values of the output in goods and services.

The same statute establishes an administrative agency called Commission on Comptrollership and Indices, whose functions are, essentially, those related to the accomplishment of the different goals included in the system. This Commission includes a representative of the central government and one of each province. The decisions made by this Commission are compulsory for the central government and for the provinces.

The taxpayers have the right to claim the refund of taxes paid, when those taxes are contrary to the system. They will be able to do this without any procedure before the Commission on Comptrollership and Indices: they can claim the refund directly, either before the courts or the administrative fiscal offices.

c. *Tax substitutive of inheritance tax*

The third system of revenue coparticipation within the Argentine's federalism, is referred to as the so-called "tax substitutive of inheritance tax". It has been in effect since January 1st., 1951, and it was enacted in order to neutralize the undesirable revenue consequences of fiscal evasion in the inheritance tax field. This evasion was particularly acute with the bearer shares of corporations; those shares were not mentioned by the taxpayers as matter taxable by the inheritance tax[17]. (See note on p. 508)

The latter tax, being direct, is established by each province. Therefore, the provinces have excluded from the scope of the inheritance tax levied according to their fiscal codes, the taxation on shares of corporations, which were inherited by the successors.

The "substitutive" tax was initially paid solely by corporations on their net wealth (suscribed capital plus reserves). But since 1962—under statute n° 16.450—also partnerships and individual merchants, both duly registered, must pay this tax on their net wealth.

The statute provides that the revenue from the tax will be distributed between the central government and the provinces according to the economic location of the assets, which are so taxed in the hands of the taxpayers.

The provinces in agreement and participating in this system, must abrogate any taxes levied upon the same taxable matter, and must reform their own inheritance taxes, excluding from their scope the assets taxed by the statute.

Finally, in order to respect the distribution criterion, the taxpayers must specify the allocation of their assets all over the country, in special forms attached to the returns.

Therefore, these returns provide the basis for the distribution of the corresponding revenue.

II. Proposals in the National Development Plan 1965-1969

The National Development Plan 1965-1969, suggests general rearrangement of all the systems of the so-called "federal coparticipation", which we have detailed above, and also the system related to the "tax on lucrative activities" (a sort of turnover tax), which is excluded from the central government participation, because it is a tax collected only by the provinces and the Municipality of Buenos Aires City.

The Plan points out that it would be necessary to correct the fact that the National Treasury has reduced substantially its participation in the ordinary revenues, due to the increase in the shares of other political jurisdictions; simultaneously it has had to enlarge the tranfers to the provinces due to other reasons, mainly by means of grants.

At the same time, the Plan adds the major financial effort that the central government will have to make for fulfilling the goals of the public investments planned. In this respect, the Plan also says that a great deal of public works will be for the benefit of regional development.

All of these are factors to be considered in a profound discussion of the share in the collection of different taxes; the new analysis would have to be on "more pragmatic grounds", says the Plan.

Finally, the Plan states that the possible bases might be the following:

a. Tendency to unify the different systems of coparticipation in tax revenues, in order to simplify the method. The only exceptions will be for those taxes which have peculiar characteristics, and justify different treatment.

b. 20 to 25% of the revenues allocated to the provinces would form a regional development fund.

c. The fund would be used for financing public works in the provinces, after a previous determination of its priority by the National Development Council and the Council of Federal Investments.

d. An Advisory Council, within the General Board of Taxation (Direccion General Im-

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17 Indeed, this "substitutive" tax was the result of a special tax treatment of the corporations and their shareholders, introduced in 1950, containing a flat rate tax on the taxable income of the corporations—it was 24%—, and a withholding tax on the dividends paid to them—it was 6%—; but the shareholders did not have to include in their income tax returns either the value of the shares which they owned, in the net wealth statement, or the dividends along with other incomes which they received.

Approved in 1951 for ten years by the statute number 14.061, the "substitutive" tax was extended ten years more by the statute number 16.450, in 1962.

positiva), with representatives from central and provincial governments will be set up. Consequently, the councils and commissions established by the different systems of revenue apportionment studies in this paper would be eliminated.

4. CRITICISM AND CONCLUSIONS

From the brief survey presented above, we can see that so far the higher portion of the total revenue related to national taxes—in the sense of its application throughout the country—still belongs to the central government. This fact has a historical explanation. About 1934, when the allocation of taxing power became a hard problem for Argentine Republic, the country was politically divided in fourteen provinces, ten national territories —all of then directly under the central government's authority—and the Federal District (Buenos Aires City). Under such a circumstances, there was certain justification for a major participation in the revenue by central government, which had to provide public services, with its own financing, in order to cover public needs for the population, not only in the Federal District but also in the national territories. But since the territories became provinces, in the years 1952 to 1957[18], the central government no longer has the duty to care for the public needs of the population in the former national territories, and in fact all of them have quite important sources to finance their own expenditures.

This is one of the reasons why the share of each level of government in the revenue was changing through time, more and more participation being granted to the provinces. But this must not be regarded as a concession from the central government, because underlying all these arrangements is the fact that the provinces are giving up their own and original taxing powers in certain areas. Nevertheless, although we recognize that the trend is favorable to the provinces, what has been done in that respect is not enough. Under the present conditions there is no justification for giving the provinces a participation lower than fifty per cent in the yield of the national taxes.

Such was the feeling of the people's representatives to the Constitutional Reforming Convention, which met in Santa Fe, in 1957. The committee specifically created to study all the proposals and bills related to the amendment of the National Constitution suggested such a solution in its report. That is to say, its proposals for amending articles 4 and 67, paragraph 2, of the Constitution implied that whenever systems of coparticipation were applied in the taxing powers between the two levels of government, the provinces must receive as a share at least fifty par cent of the revenues[19]. Unfortunately, due to political troubles, the bill of amendments included in that report was only partly dealt with by the Convention.

Besides, there is another very important circumstance, which has only partially been kept in mind by all the statutes and agreements related to the taxing power problem. We are referring to the encouragement of "poor provinces" to achieve better economic and financial conditions in their provincial developments. To a certain extent this was taken into account by statutes 14.390 and 14.788 (see paragraph 3, point 1, A.,

18 Article 30 of National Constitution makes possible the setting up of new provinces.

19 "Argentine Republic. Diario de Sesiones de la Convencion Nacional Constituyente", Buenos Aires, 1957, volume II, pages 1016 and 1021.

point b, and point II). But it is necessary to go further. The differences in many respects between rich and poor regions are, sometimes, so deep and great, that is undeniably necessary to reduce them. This is an action which merits attention and—of course—is a problem the responsibility for which belongs both to central government and to the rich provinces.

Finally, from the economic standpoint we can add other consideration, which is pointed out by respectable students in public finance. This consideration results from the analysis of multilevel financial systems, peculiarly significant for federalism. In such analysis a very important place is taken by what is known as equalization policy among the regions of a country. The purpose of this policy is to provide for all of them the same benefits through the activities accomplished by public entities[20].

The achievement of this objective would also help to strengthen the federal system in the country. Federalism is a substantial and far-reaching base, upheld by the National Constitution in its First Article; it is a base founded in strong and deeply rooted historical principles.

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O.P. CHAWLA:

INTEGRATION OF ESTATE AND GIFT TAXES: A CASE STUDY OF INDIAN AND CEYLONESE TAX LAWS

I. INTRODUCTORY

Professor Nicholas Kaldor went to India in 1956 and to Ceylon in 1958 and recommended the adoption of an integrated direct tax structure by their Governments along almost identical lines. One of the integral parts of these recommendations was the introduction of a general gift tax in substitution of the then existing estate duty in both the countries with a view to substantially attain the identical objective of reduction of in-equalities of income and wealth and of opportunity. Such a tax would prevent avoidance of estate duty by plugging the most common loophole, viz., gratuitous transfer of property during one's life-time. The Governments of both the countries seemed to acquiesce in this major recommendation. It is interesting, therefore, to follow through the subsequent developments in these countries (which possessed so much of common background) in the area of estate and gift taxes and find that while one country, almost faithfully, followed the Kaldor recommendation, the other moved towards it haltingly, hesitantly and erratically and was still a long way off.

Developments in this field in India shall first be detailed; those in Ceylon shall then be explained. In the end, a comparison shall be instituted to draw some conclusions.

II. ESTATE AND GIFT TAXES IN INDIA

Estate duty was levied in India in 1953 to rectify "unequal distribution of wealth... to a large extent". Estates in excess of Rs. 1,00,000 were subjected to tax. A number of exemptions were provided. Tax rates ranged from 7.5 per cent on the first slab to 40 per cent on the last, viz., the value of estate above Rs. 50 lakhs (10 lakhs= 1 million). In the absence of a gift tax which the Taxation Enquiry Commission (1953-54) had thought to be administratively non-feasible at that time, the estate duty could not have played the role assigned to it. An improvement was recorded when a gift tax was imposed in 1958 on the recommendation of Kaldor. The statement of Objects and Reasons to the Gift Tax Bill, 1958, read: "Gifts from one person to another provide a convenient means of avoiding or reducing liability to estate duty, income-tax, wealth-tax and expenditure-tax. The only effective method of checking such attempts... is by levying a tax on gifts." The Gift Tax Act provided for a number of exemptions some of which considerably eroded the tax base. One of these exemptions was in respect of a gift to spouse subject to a maximum of Rs. 1,00,000 in aggregate. The law also provided for a tax-free slab of Rs. 10,000. In the same year, the tax-free slab in the estate duty rate structure was reduced to Rs. 50,000.

Short of fully integrating gift and estate taxes, the best alternative would be to keep gift tax rates steeply higher than estate duty rates on comparable slabs of property so that they could serve as some sort of a deterrent to gratuitous transfers before death. However, the gift tax law failed to accomplish this as is obvious from Table 1 which compares gift tax and estate duty rates.

TABLE I: Estate Duty and Gift Tax Rates: 1958-59 to 1963-64.

Slabs of property (next to tax free slabs)		Rates per cent	
		Estate Duty	Gift tax
Next Rs.	50,000	4	4
,,	50,000	6	6
,,	50,000	10	8
,,	50,000	12	10
,,	50,000	12	12
,,	50,000	15	12
,,	150,000	15	15
,,	50,000	20	15
Next Rs.	450,000	20	20
..	50,000	25	20
,,	950,000	25	25
,,	50,000	30	25
,,	950,000	30	30
,,	50,000	35	30
,,	1950,000	35	35
,,	50,000	40	35
On the balance (above Rs. 50 lakhs).		40	40

Note: Slabs have been cut up to present a comparative picture of rates.

On the whole, the gift tax rates were lower than estate duty rates. Even if the gift tax rates were identical to or even slightly higher than estate duty rates, these could not prevent tax avoidance and serve the equalitarian purpose. In view of two taxes operating separately, having separate exemptions, separate exemption limits and separate rate structures, it was always profitable to transfer property partly by way of gifts inter vivos year after year and partly by way of bequests.

The two tax laws were amended in 1964. Proposing the amendments, the Finance Minister observed: "I propose to completely recast the tax rate schedule of Estate Duty and Gift Tax... The social purposes connected with these two taxes have somewhat been haltingly reflected in the rate structure that now obtains... The Gift Tax was introduced as a complement to Estate Duty in order to deal with gifts which ultimately have the effect of reducing the value of the estate subject to duty. ...If there is to be a limit on the amount of wealth to be passed on from one generation to another, we cannot escape from dealing with gifts which can be used as a means of avoiding or reducing the liability to the impact of Estate Duty." The changes made in the two tax laws were: (1) The exemption limit of gifts was reduced to Rs. 5,000; (2) Excempt amount of gifts to spouse over life-time was reduced to Rs. 50,000; (3) A principle whereby gifts made to the same donee over a period of 5 consequtive years were to be aggregated to determine the gift tax rate applicable to a gift in one of those years was introduced; (4) Rates of estate duty and gift tax were revised to reverse the earlier relationship between them. This is brought out in Table II.

TABLE II: Estate Duty and Gift Tax Rates: 1964-65 and 1965-66.

Slabs of property (next to tax-free slabs)		Rates per cent	
		Estate Duty	Gift Tax
Next Rs.	5,000	4	4
,,	15,000	4	8
,,	25,000	4	15
,,	5,000	4	25
,,	95,000	8	25
,,	5,000	8	40
,,	195,000	15	40
,,	105,000	15	50
,,	500,000	25	50
,,	500,000	40	50
,,	500,000	50	50
On the balance (above Rs. lakhs)		85	50

Note: As in Table I.

These changes integrated the estate duty–gift tax laws to a degree. But still a donor could, with a little of estate planning, transfer large segments of his property and avoid a substantial amount of his prospective estate duty. However, even this slight improvement was not allowed to last more than 2 years as in 1966 the new Finance Minister took a regressive step by amending both the tax laws as under: (1) the exemption limit for gift tax was again raised to Rs. 10,000; (2) The aggregation principle was abolished; (3) The gift tax rates were revised downwards while estate duty rates on a few intermediate slabs were raised as shown in Table III.

The Finance Minister expressed the rationale for making these changes thus: "I propose to revise the rates of Gift tax in order to bring them more closely in line with the rates of estate duty. In the process, the rates applicable to different slabs of value of gifts are also being reduced... I also propose to delete the provision for the aggregation of the value of gifts to the same donee over a number of years... it is a measure whose practical utility is not established, specially if the time and trouble it involves on the part of both the administration and the assessees are taken into account."

TABLE III: Estate Duty and Gift Tax Rates: 1966-67 and 1967-68.

Slabs of property (next to tax free slabs)		Rates per cent	
		Estate Duty	Gift Tax
Next Rs.	15,000	4	5
,,	25,000	4	8
,,	10,000	4	10
,,	40,000	10	10
,,	50,000	10	15
,,	10,000	10	17.5
,,	40,000	15	17.5
,,	110,000	15	20
,,	40,000	25	20
,,	110,000	25	25
,,	40,000	30	25
,,	460,000	30	30
,,	40,000	40	30
,,	460,000	40	40
,,	40,000	50	40
,,	460,000	50	50
On the balance (above Rs. 19.5 lakhs).		85	50

Note: As in Table I.

It is obvious, in view of the irrational arguments put forward, that the real purpose was to undo the slight improvement in the direction of the integration of the two taxes brought about in 1964. During 1964-66, gift rax rates were higher than the estate-duty rates until the property-level of Rs. 1,450,000 was reached and therefore the effective gift tax rates were higher than the effective estate duty rates much beyond this level. At present, gift tax rates are higher than the estate duty rates upto Rs. 310,000 level only; these are equal at the 350,000–460,000 level; the estate duty rates are higher than the gift tax rates beyond this level. As a result, both in absolute as well as relative terms, the more rich can effect much more tax avoidance than the less rich. Table IV is

set out to show the relative extent of estate duty-avoidance possible at a few levels of estate under the three rate schedules which have operated during the last 10 years.

TABLE IV: Extent of Saving in Estate Duty by making a single gift during 1957-58—1966-67 at a few levels of Property owned by Individuals. ('000 Rs).

Level of property	Property transferred	1957-59 to 1962-63			1963-64 to 1964-65			1965-66 to 1966-67		
		Saving in Estate duty	Gift Tax payable	Net saving or loss	Saving in Estate duty	Gift Tax payable	Net saving or loss	Saving in Estate duty	Gift Tax payable	Net saving or loss
100	10	0.4	—	0.4	0.4	0.2	0.2	0.4	—	0.4
500	10	1.5	—	1.5	1.5	—	1.5	2.5	—	2.5
	250	36.0	8.2	27.8	37.5	50.15	12.65	52.5	24.0	28.5
1000	250	50.0	8.2	41.8	62.5	50.15	12.35	75.0	24.0	51.0
	500	100.0	39.5	60.5	125.0	185.15	60.15	150.0	79.0	71.0

Note: The calculations in this table take into account the maximum tax-free gift which could be made to spouse by a donor, viz., Rs. 1 lakh upto 1962-63 and Rs. 50 thousand thereafter.

It would be seen that substantial estate tax avoidance could accrue through the gift-device during the whole of the period under study except during 1963-65 when large gratuitous transfers could invite a penal gift tax. A more realistic estate planning shall call for the spreading of gifts over a number of years. Table v is therefore constructed to show the extent of saving in estate duty if certain amounts of gift were made over a period of 5 years (in five equal instalments). The position then changes even for the years 1963-65, yielding large savings to the donors (and the donees, eventually). It would be observed both from Tables IV and V that the present (1965-67) estate duty—gift tax rate differentiation is even wider than the corresponding differentiation during 1957-63, thus yielding a still wider loophole.

TABLE V: Extent of Saving in Estate Duty by making Gifts over a 5-year period during 1957-58—1966-67 at a few levels of Property owned by Individuals.
('000 Rs).

Level of Property	Property transferred	1957-58 to 1962-63			1963-64 to 1964-65			1965-66 to 1966-67.		
		Saving in estate duty	Gift Tax payable	Net saving or loss	Saving in estate duty	Gift tax payable	Net saving or loss	Saving in estate duty	Gift Tax payable	Net saving or loss
100	10	0.4	—	0.4	0.4	—	0.4	0.4	—	0.4
500	50	7.5	—	7.5	7.5	—	7.5	12.5	—	12.5
	250	36.0	4.0	32.0	37.5	18.25	19.25	52.5	9.75	42.75
1000	250	50,0	4.0	46.0	62.5	18.25	44.25	75.0	9.75	65.25
	500	100.0	16.0	84.0	125.0	75.75	49.25	150.0	33.75	116.25
	800	142.0	37.0	105.0	170.0	150.75	19.25	210.0	76.25	133.75

Note: As in Table IV.

This see-saw battle of the estate duty and gift-taxes rates might now be set against the corresponding position in Ceylon.

III. ESTATE AND GIFT TAXES IN CEYLON

In Ceylon, the Personal Tax Act was passed in 1959 which, inter alia, introduced a gift tax for the first time. It exempted gifts in consideration of marriage of a defendent (S) upto Rs. 10,000 and gifts to approved charities if their value exceeded Rs. 1,000, subject to a maximum of Rs. 300,000 during the life-time of the donor. The exemption limit was fixed at Rs. 2,000. The rate schedule started at 5 per cent applicable to the first Rs. 50,000 and rose progressively by 15 steps to 100 percent on taxable gifts beyond Rs. 1,440,000. This rate schedule was to apply to all gifts made by the same donor over his life-time irrespective of the year in which the gift was taxed. It meant that all taxable gifts (made after July 17, 1958) were to be aggregated, the latest year's gifts being then taxed at the marginal rate applicable. The estate duty was fully integrated with the gift tax. All taxable gifts made during the life-time of the donor (after July 17, 1958, of course) plus the gift tax thereon were to be included in the taxable estate of the decendent. The exemption limit for estate duty was Rs. 20,000. The taxable estate was to be subjected to a rate schedule starting with a rate of 5 per cent on the first Rs. 30,000 and rising progressively by 15 steps to 50 per cent on the value of estate in excess of Rs. 2,130,000. The gift tax rates were much higher than the estate duty rates.

The Personal Tax Act was replaced by the Inland Revenue Act in 1963 which is in force at present. Applicable to gifts made after July 31, 1963, it exempts gifts upto Rs. 1,000 a year only. Moreover, where the aggregate gifts in a year exceed Rs. 1,000, the entire value of the gift is liable to gift tax. The rates of gift tax have been raised further on intermediate slabs. The rates of estate duty have also been raised, the top rate being 70 per cent applicable to the value of taxable estate above Rs. 2,480,000. The gift tax rates remain higher than estate duty rates at all levels. No tax avoidance is possible through the making of gifts. In fact, the total gift tax paid by a donor over his life time might very well exceed the total estate duty payable on his estate, thus yielding a tax refund.

IV. CONCLUSIONS

The extreme divergence in the tax laws of the two countries from the integration angle makes the job of drawing conclusions on a comparative basis easy:

1) The Indian estate and gift taxes provide for more and high exemptions; the exemption limits of both the Indian taxes are also higher.
2) The estate duty rates in Ceylon are higher than those in India except those on the top brackets; the gift rates in Ceylon are also higher than those in India.
3) The estate duty rates are higher than the gift tax rates in India; the gift tax rates are higher than the estate duty rates in Ceylon.

4) In Ceylon, gifts by a donor are aggregated over his life-time for gift tax purposes and area added to estate at death for estate duty purposes. There is thus perfect integration, leaving no room for tax avoidance. The gift tax operates separately from estate duty in India and there is no integration between them; as a result, careful estate planning can yield high returns in the form of huge tax avoidance.
5) The estate and gift tax structure in Ceylon is perfectly aligned to the country's socio-economic objective; it is just the reverse in India, causing a wide gap between the ideal and the reality.

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concerning industrial, commercial or scientific experience. Special attention is paid to the avoidance of double taxation arising from such agreements. Suggestions for tax incentives provided for by developed countries with regard to such agreements concluded with enterprises in developing countries as a private contribution to economic development aid is appended.

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By order of the "Bundesministerium für wirtschaftliche Zusammenarbeit" the "Forschungsstelle für Internationales Steuerrecht" in Munich has prepared a new series of publications entitled Schriftenreihe "Steuern in Entwicklungsländern" published by Verlag Neue Wirtschafts-Briefe, Herne-Berlin. These publications are designed to inform German business enterprises on the tax structure of less developed countries. In separate publications, each pertaining to one specific country, a survey is given on taxation problems arising from capital investments in, or loans to, or royalty agreements granted within a less developed country. These publications will be updated through the publication of substantial changes in the "Internationale Wirtschafts-Briefe" issued by the same publisher.
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EDITORIAL:

THE CARTER REPORT

The May 1967 issue of the Bulletin contained a summary of the findings and proposals contained in the Report of the Canadian Royal Commission on Taxation, the so-called Carter Report. This report, the culmination of four years of study, includes many recommendations for far reaching and indeed "revolutionary" changes in the Canadian tax system.

Thus the Carter Report sparked a still continuing debate about the merits of the proposals contained therein and consequently about the merits of the present Canadian tax structure.

In conjunction therewith the Bulletin takes pleasure in publishing Prof. Harris's comprehensive analysis and criticism of the Carter Report, "What Should Canada Do With the Carter Report?".

It is our opinion that the continuing debate will be beneficial not only to Canada but also to all nations through its enrichment of those bodies of knowledge which deal with the raising of governmental revenues, public finance and taxation.

Certain principles and techniques of taxation have gone unquestioned for too long. The critical examination resulting from the debate will either again reveal their inherent validity or lead to a consensus in favor of seeking alternatives to them and in that way provide the basis for the improvement of tax systems throughout the world.

DR. J. C. L. HUISKAMP

* * * * ARTICLES * * * *

EDWIN C. HARRIS:*

WHAT SHOULD CANADA DO WITH THE CARTER REPORT?

THE REACTION TO DATE

When the Report of Canada's Royal Commission on Taxation[1] was released to the public late in February 1967, the first reaction tended to be one of stunned surprise: the Report was of imposing bulk, and its contents were more radical and were more of an integrated single "package" than most tax specialists had anticipated. Some vehement opposition emerged almost immediately, particularly from industries whose specially favored tax status the Report had recommended should be removed; and this kind of criticism has in no way abated some eight months later. Others, however, who wished to make a serious effort to evaluate the Report objectively felt that it would take much time, thought, and debate before constructive appraisal could emerge. When the Canadian Tax Foundation held a conference late in April devoted entirely to the Report, many of the speakers admitted that they had not yet had a sufficient opportunity to digest the Report and to reach sound conclusions on its merits. It has only been in the fall, as numerous briefs have been prepared for submission to the Minister of Finance to meet the October 31 deadline set by him,[2] that viewpoints have begun to crystallize and constructive overall analysis to take shape.

Certain patterns of approach have emerged in the increasing number of briefs and published works purporting to deal with part or all of the Report.[3] A favorable initial impression was made on most commentators: they were taken by the apparent comprehen-

*) Faculty of Law, Dalhousie University, and of the firm of Daley, Black, Moreira & Piercey, Halifax, Canada.

1. The "Carter Report", as it is commonly known, from the name of the chairman of the Commission.

2. As a preliminary before issuing a government White Paper around the beginning of 1968, followed by a further public debate and ultimately by an income tax amending bill in Parliament later in 1968.

3. Many briefs, press comments, etc. are not readily available. The documents and materials that are available include the Report itself (6 volumes plus an index volume and also a volume of press releases); the studies prepared by the Commission's research staff (27 in all, of which 18 were received to the date of writing); a summary of the recommendations of the Commission, published by CCH and also reproduced in 15 Can. Tax J. 79–219; Report of Proceedings of the 19th Tax Conference, Canadian Tax Foundation; Robertson, A Perspective on the Report, 15 Can. Tax J. 230; Brazer, Review of the Report, 15 Can. Tax J. 273; Goodman, Estate Planning under the Royal Commission Proposals, 15 Can. Tax J. 303; Fact and Opinion, 15 Can. Tax J. 341-45; Musgrave, An Evaluation of the Report, 15 Can. Tax J. 349; Jones, The Report of the Royal Commission on Taxation: An Analysis, 5 Alta. L. Rev. 174; Petrie, A Review of Some Critical Issues in the Report of the Royal Commission on Taxation, Canadian Chamber of Commerce; CCH series of booklets on the Carter Report (13 were published to the date of writing); McDonald, Carter Report Studies, Butterworths (1 was received at the date of writing); Asper, The Carter Report, Equitable Income Tax Foundation (6 studies). All these materials were published in 1967. There have been many other magazine and journal articles, and there will be many more.

siveness of the Report, the sweep of its logic, the boldness of its design, and the clarity and forthrightness of its expression; the Report seemed to provide clear-cut and relatively simple solutions to some of the most vexing problems of the present Canadian tax system. But the Report has not worn well. To many who have patiently considered and sifted the flood of criticism that it has provoked, its apparent virtues are now seen to reflect superficiality, theoretical abstraction, an ignoring of pertinent problems, and a refusal or inability to come to grips with the practical implications of its proposals. It is not hard to add one's own voice to the critical chorus, which now seems to have the field largely to itself, while defenders of the Report, to the extent that there are any left, are almost silent.[4] As the Carter edifice appears to crack, crumble, and collapse before the heavy and sometimes bitter onslaught of criticism, Canada seems to be further than ever from an acceptable solution to its tax problems. If the Report has done nothing else, it has shown ample reason for dissatisfaction with the present tax system; at the same time, many are convinced that the proposed system, if it could implemented without modification, would be even worse.

DANGERS TO BE AVOIDED

In the present confusion two alternative dangers may be identified. The first is that the Report will be wholly or substantially implemented by a harrassed and frustrated government that is not prepared to refer the whole matter back to another royal commission to sort out the valid parts from the invalid and that may also hope for some political support from the "little men", whom the Report is supposed to help. The opposite danger is that the Report will be largely or completely discarded, thereby losing the benefit of some most worthwhile recommendations. The government in this situation clearly needs something more than destructive criticism—valid as that may be in the circumstances. Alternatives to unacceptable proposals must be suggested, though it is difficult for individuals and groups, on the basis of a few months' consideration, to develop an integrated and detailed new system when it took the Commission and its large staff some years to go through a similar process. It may be hoped that a comparatively limited number of modifications, albeit fundamental, to the "package" proposed in the Report would enable the government to adapt and build upon large parts of the work done by the Commission and, with some subsequent concentrated expert study and public debate, to devise a new and much more acceptable system.

THE APPROACH TO BE FOLLOWED HERE

This paper will attempt to show in a summary and quite condensed form why many of the Report's recommendations are unsound, unworkable, or otherwise inadvisable. In many cases an alternative approach will be suggested, building wherever possible on the work of the Commission! Of course, such an alternative system can be simply a starting point for further discussion and analysis and is not put forth as a finished-product substitute for the Carter "package".

4. There may be a tendency to overrate the extent of the opposition, which has come mostly from groups that are knowledgeable or articulate. The "little man", who has great difficulty understanding what the Report is about, may still have the impression that the Report would lower his taxes and "soak the rich". Because the "little men" have many votes, the government must take this into account

Many specialized and technical aspects of the Report and of the present tax system will not be considered.[5] The following analysis will assume that the reader is familiar with the main recommendations in the Report.[6]

GENERAL AND PHILOSOPHICAL

Even severe critics of the Report tend to be impressed by its logic; but this logic is more a matter of form than of substance. That there are many flaws in the consistency of the grand design becomes apparent when the full significance of numerous arbitrary rules and special cases is realized. Thus, the arbitrariness of an annual measurement of income coupled with progressive personal income tax rates, the failure to provide for taxation of unrealized or imputed gains, and the uncertainty as to treatment of mortality gains and losses on life insurance all detract from the consistency of the system. The logic and symmetry of the Report seem to be most in evidence in picayune matters, where burdensome rules are often advocated for the sake of consistency. Many of the early converts to Carterism are now somewhat sadder and wiser; and the earlier prevailing view—that expediency, approximate fairness, and administrative feasibility must be prime criteria under any tax system—seems to have been reinforced and clarified.

By a process of highly abstract (and admittedly arbitrary) reasoning, the Report adopts "equity" as the chief criterion for its proposed system; equates equity with taxation in accordance with ability to pay; and concludes that ability to pay is measured by "discretionary economic power", which is defined (again purely arbitrarily or subjectively) as the portion of a tax unit's total economic power that is available for discretionary use—*i.e.*, does not need to be used to maintain the unit at a reasonable standard of living that will take into account not merely the size and composition of the unit but also its level of income. Total economic power is to be measured by the annual increase in economic power of the tax unit, in other words its "income" in the sense of a comprehensive tax base (c.t.b.). To the extent that there are questionable assumptions in the foregoing chain of reasoning, the theoretical foundation of the Report is weak.

Thus, most observers would maintain that ability to pay depends in part upon liquidity, yet the Report often ignores or belittles the difficulties faced by a tax unit whose holdings are not and cannot readily be made liquid. Furthermore, ability to pay would seem to depend not on an arbitrary annual measurement of increment in economic power but on the tax unit's total economic power or wealth. True, the Report gives some reasons for not imposing a wealth tax as such, but in so doing it departs from what most people would consider ability to pay. The concept of discretionary economic power is even more questionable as a theoretical justification for what is in reality an arbitrary tax rate structure. The Report proposes to tax all "discretionary economic power" at 50%, on the basis that each successive bracket of income has a higher component of discretio-

5. While I am indebted to other commentators for many of the criticisms that I shall raise, it is impracticable in most cases to cite specific references. Many of the points are made again and again in the published commentaries, with slight variations.

6. In addition to the references cited in note 3, the reader will find useful though brief summaries, based on Commission press releases, in XXI Bulletin 179 & 201 (April & May, 1967). These later summaries should suffice as background for this paper.

nary economic power, until all taxable income over $ 100,000 per annum is deemed to be discretionary. This approach is one of mere expediency: if pure equity is to be the criterion, it would seem to require equality, which would imply that, after allowing tax-free the minimum level of income necessary to maintain the tax unit, the government's taxing and expenditure functions would be used to equalize the economic position of all tax units. Of course this pure equity would not be acceptable to the Commission, nor would it be politically acceptable in Canada; but the Report's concept of "discretionary economic power" should be recognized as departing from equity—presumably for reasons of incentive, reward, and other non-equity factors. Often (though not always) the Report appears to apply the concept of ability to pay to the income tax or even to a part of the income tax in isolation, without regard to the effect of the rest of the tax system or of the government expenditure system. As a result of this series of inconsistencies and compromises, the recommended system is unlikely to impose tax in proportion to what most Canadians would consider ability to pay, nor would they necessarily want the tax system to do so. Too much lip-service has been paid to the equity criterion, while other criteria, though implicitly present, are not clearly enough identified or directly taken into account.

The Report seems to look with favor upon a growing role of government, particularly at the federal level, in the management of the economy. This attitude has provoked bitter criticism from some groups to the effect that the Report is a "socialist" document and will lead to the destruction of the economic liberties, and perhaps also the political liberties, of Canadians. Some of the language in the Report does suggest that there has been a prejudgment of highly political questions; but on the whole no greater degree of government intervention in the economy is contemplated than can be found in almost any developed country outside North America, and here the Report is probably indicating accurately the way that Canada must soon follow. There is, however, a justified fear that too rapid implementation of the Carter economic program, before there has been a corresponding increase in economic knowledge and sophistication, could seriously disrupt the economy. The frequently heard criticism that the Report proposed its "package" to the Canadian government on a take-it-or-leave-it basis is probably unfair. The Commission is to be commended for attempting to fit the various parts of its system together in an integrated fashion, instead of simply suggesting piecemeal and uncoordinated amendments to the present system. This means, however, that if any key part of the "package" is rejected or materially modified, the rest of the "package" must also be re-examined and probably modified. Unfortunately the Commission has given almost no guidance as to how we might proceed if parts of the "package" are not acceptable, but to do so would have made the Report unconscionably long. It is therefore with much reluctance that most tax specialists have had to conclude that the Carter "package" is not an acceptable alternative to the present tax system. At least some of the Report's recommendations, however, including many of those relating to measurement of business income, government fiscal policy, sales taxation, and administrative and judicial reforms, can be considered apart from the "package".

The Report seems to have found more support among economists than among accountants, lawyers, and other tax practitioners, though most economists find fault with at least some of the Report. It is not surprising

that the Report has more appeal for economists, since it is fundamentally an economist's document. It takes an economist's approach to tax questions and seems to be primarily concerned with the aspects of taxation that most interest economists; it is correspondingly weak in its appreciation of the practical tax problems faced by lawyers and accountants. Because of its tendency to take an "overview" of the tax system, the Report frequently underemphasizes or ignores the situation of the individual taxpayer. Since lawyers and accountants are concerned almost entirely with the individual taxpayer, to them the Report appears unrealistic and theoretical.

As well, the tone of the Report antagonizes many readers. Often its recommendations are advanced in a way that suggests their inevitability—wich appears presumptuous when the weakness of some of the premises is shown. There is a strong moralistic overtone, leading to the advocacy of strict and burdensome rules in order to prevent possible tax avoidance by a few taxpayers. As one somewhat exasperated legal commentator put it, "The Report is stern, uncompromising, ungenerous, tight-fisted and mean."[7] There is a tendency not only to advocate harsh rules to keep taxpayers in line but also to threaten even harsher treatment "if substantial tax avoidance results".[8] Even where a recommendation made in the Report seems sound, there is a tendency to overstate the case to the point of weakening the force of the recommendation.

Another consequence of the economist's bias in the Report is that to the tax practitioner most of the Report is hopelessly vague and imprecise, and in many important areas it is disappointingly incomplete. There is a tendency to persistent superficiality at the technical level. The inference of completeness and thoroughness that some have drawn from the massiveness of the Report and its supporting studies is unsound, because much of its bulk is attributable to a remarkable degree of repetition and to a substantial amount of general economic discussion. Many of the staff studies are irrelevant or peripheral, because they were prepared before the Commissioners' ideas had crystallized, so that most of the studies do not provide additional reasons and technical underpinning for the Report. Even the faults of the present tax system are only partially and often superficially explained. Many practitioners may justifiably feel that the time and energies of the Commissioners and their staff would have been more productively employed, for example, in rationalizing and coordinating such technical provisions in the Income Tax Act and Regulations as those relating to depreciation, which abound in loopholes, ambiguities, contradictions, obscurities, and lacunae; instead the Report does little more than to suggest that the present system for claiming depreciation allowances be continued.

ECONOMIC ASPECTS

While the economic aspects of the Report have earned it praise from economists, some economists feel that its predictions of the economic consequences of its recommendations are presented with an unjustified degree of assurance, having regard to the limited state of economic knowledge on the incidence of taxes and on the likely reaction of the national and international economy to substantial tax changes in Canada. The Report concludes that its recommendations

7. Gibson, Gifts, Including Inheritances, in Can. Tax Foundation, Proceedings 19th Tax Conf. 270, 271 (1967).

8. A typical example is found in the discussion of tax havens at vol. 4 p. 521.

would slightly reduce business and private saving but that this would be more than offset by an increase in government saving. To anyone who is familiar with the phenomenal rate of growth of expenditures of all levels of government in Canada this static kind of analysis, based on 1964 economic data, seems irrelevant: for the indefinite foreseeable future all Canadian governments can be expected to spend all the revenues they can get, and more. For the same reasons the suggestion in the Report that after a few years federal government revenues would rise so rapidly under the proposed tax system that it will be both possible and desirable to reduce tax rates, so as to avoid "fiscal drag", seems almost ludicrous.

With the appearance of the Report, Canada has had to endure the arguments and counterarguments, with which most other countries became familiar long ago, concerning the effect of capital gains taxation on incentives, risk taking, and economic growth. No attempt will be made here to summarize the arguments. For various historical reasons the taxation of capital gains is coming to Canada somewhat later than to most other developed countries; but almost surely it must come now. Undoubtedly, other things being equal, risk taking, investment, and productive activity in general can be adversely affected by capital gains taxation, or indeed by any taxation; but experience elsewhere, particularly where capital losses are deductible, indicates that capital gains taxation will not materially impair economic growth. It is not sufficiently recognized that, to a substantial extent, what elsewhere would be considered capital gains are already taxed in Canada as ordinary income—particularly recaptured depreciation and virtually any transaction involving the purchase and sale of real estate other than the taxpayer's own residence. Apart from transactions in corporate shares, where there is still some scope for capital gains (though even here diminishing in extent), virtually every gain made in the course of carrying on a business or a businesslike activity or in a transaction having as one of its main purposes the realization of gain is taxed as income, often at the top corporate rate or at high progressive individual rates. Except for share transactions capital gains are recognized only when they occur almost unexpectedly, usually because of the frustration of a purely investment intention. Almost every risk-taking venture will now attract tax if successful, and so it is misleading to assert that the immunity of capital gains from taxation encourages risk taking in Canada. The Report's recommendation that capital gains in all forms be taxed seems in general to be sound and would have the merit of treating all gains alike, avoiding loopholes by which a taxable kind of gain can be transformed into a nontaxable kind, and avoiding the inequity of allowing unusual and unexpected gains to go tax-free.[9] Similarly, capital gains are income just as much as any other kind of gain and in principle (as well as for administrative convenience) should not be separately identified or taxed at preferential rates. The real issues seem to be to identify the amount of gain, to avoid imposing a tax on capital in the guise of an income tax, and to ensure (by income averaging or otherwise) that the use of a progressive rate structure together with an annual measurement of income does not result in punitive rates of tax on irregularly recurring gains; on all these matters the Report is less satisfactory.

9. It seems apparent, however, that the Report has greatly overestimated the amount of net additional capital gains that would be brought into the tax base, particularly if, as I shall later recommend, the inflationary element in these gains is eliminated.

Many observers find the Report to be particularly naïve and unsound in its proposals relating to Canada's international transactions. The Commission anticipates that, while nonresident investors would be induced to sell their holdings of Canadian shares because, as a result of the integration[10] system (which benefits only Canadians), the price of the shares would rise too high in relation to their yield, they or other nonresidents will also be induced to buy Canadian debt securities, which would be more attractively priced in terms of yield. Too much equity capital is specifically committed to equities or even to equities in a particular industry for this kind of transference to take place directly on any significant scale; and the fact that Canadian governments have been absorbing almost every available dollar of foreign investment in Canadian debt makes it unreasonable to expect that Canadian corporations would obtain substantial debt financing from abroad. Where Canada is bound by a fixed exchange rate and by commitments to the United States concerning the level of its foreign exchange holdings, the Canadian government's room for maneuver is limited if there is a substantial net movement of foreign capital. Ironically, where growth rather than yield is the chief reason for investment, Canadian shares might prove more attractive to nonresidents, who would not be subject to Canadian capital gains tax, than to residents.

The Report concludes that tax neutrality between residents and nonresidents is impossible and abandons any attempt to achieve even a measure of neutrality. Instead it proposes to use the tax system to induce Canadian residents to displace nonresidents as the holders of Canadian equities, while at the same time not absolutely worsening the position of foreign investors who retain their investment. Unquestionably the possibilities for attaining international tax neutrality are limited,[11] but it does not follow that the neutrality criterion should be completely ignored. The assertion in the Report that the proposed system will not prejudice foreign investors (apart from those who have invested in the extractive or life insurance industries) ignores the adverse effect of the elimination of the low rate of tax on the first $ 35,000 of taxable corporate income, the increased withholding taxes on certain kinds of remittances to nonresidents, the taxation of all corporate capital gains at 50%, and the likely influence of integration on corporate pricing and dividend policies.[12] Foreign holders of Canadian shares who chose to realize their investment would reap a windfall because of higher share prices attributable to integration, while those who retained their Canadian shares would be adversely affected. While retaliatory measures by foreign governments cannot be ruled out, most of the disadvantages to Canada of implementing the international aspects of the Report would be inflicted simply by the operation of the market. The political objective of making it attractive for Canadians to "buy back their own corporations", which in many key industries are controlled by foreign investors, would not be furthered by the proposed tax measures any more than it has been by other tax measures attempted in the past:[13] some portfolio investors, whose capital

10. This term is used to refer to the recommended system of integrating corporate and personal income taxes for Canadian resident individuals.

11. Even neutrality at the domestic level has limits that the Report does not seem to recognize.

12. See the remarkably shallow discussion at vol. 4 p. 32.

13. See generally Harris, Canadian Taxation of Branches and Subsidiaries of Foreign Enterprises, XIX Bulletin 441 (1965).

investment is economically advantageous and not politically objectionable to Canada, would be induced to sell, but nothing in the Report is likely to lead foreign direct investors to sell control of their Canadian subsidiaries to Canadians. By the limits it places on the claiming by Canadians of foreign tax credits and its excessive concern with the use of tax havens and by its willingness to impose much higher withholding taxes on income flows from Canada to nonresidents, the Report takes a narrow, nationalistic view of Canada's international economic relations. The flow of capital and persons both ways would be discouraged—and probably to a much greater extent than the Commission contemplated. Canadian growth and development would be far better served by not imposing artifical tax obstacles in the way of international trade and investment.

The Report displays a degree of confidence in the capacity of the federal government to pursue effective stabilization policies, even without provincial cooperation, that may be entirely unwarranted, having regard to existing balance-of-payments constraints on the use of fiscal and monetary policies for stabilization purposes. Some economists feel that the Report, instead of its unrealistic emphasis on "fiscal drag", should have devoted greater attention to stabilization problems that would accompany implementation of its proposals and that would arise from time to time thereafter. Until there is reason for assurance that the federal government can neutralize any substantial economic fluctuations that would result from the immediate establishment of a radical new tax system, any such sustem should be introduced on a gradual basis over a period of years.

THE CONCEPT OF INCOME

The Report's view that income should be defined in a comprehensive way and that existing artificial distinctions between ordinary income and capital gains should be eliminated is basically sound. Apart from special problems relating to the integration proposal, the determination of a basis (the Report persists in using the inappropriate term "cost basis") for each asset that is subject to a gains tax will be necessary. Inevitably this proposal will create substantial transitional problems of valuing assets that are on hand at the implementation date and that are not readily marketable. The Report recognizes these difficulties and in some cases proposes alternative procedures to actual valuation. Nevertheless, in the case of assets that are not readily marketable the problems of establishing original cost, the cost of subsequent capital improvements, and even the date of acquisition may be so great as to force an actual valuation because the necessary data cannot be established to permit use of the averaging alternative. The proposal that, where the taxpayer elects to average the gain over the period before and since the implementation date, the maximum prior period for averaging should be ten years is ungenerous for long-lived assets; and the severe problem of inflationary gain, particularly for such assets, is here, as elsewhere in the Report, ignored. The transitional problems could be substantially alleviated by permitting averaging from the actual date of acquisition and by giving effect to the suggestions that will be made later to eliminate from the tax system all assets held for personal use and to permit full correction for inflation.

In at least three respects, because of the way the c.t.b. is defined, the Report in effect would impose a tax on capital in the form of a tax on income—the treatment as income of (1) gratuitous transfers; (2) inflationary gains; and(3) compensation for loss of life or of

earning capacity. This would have devastating effects on capital formation and retention. Here the "logic" of the c.t.b. seems to blind a majority of the Commission to the oppressive nature of such a tax and its pernicious economic consequences. Of the three foregoing categories, the most serious would be the taxation as income of gratuitous transfers (i.e., inter vivos gifts and transfers of property on death).

Because the Report uses "ability to pay" more as a slogan than as a consistent principle, its "logical" extension of the c.t.b. to gratuitous transfers is at least open to question. Most Canadians now consider these transfers to be a means of preserving capital rather than an addition to income. Taxing these transfers as income would lead to disinvestment once every generation, would impose a shockingly high tax burden on small estates and, combined with a deemed realization to the transferor of appreciated property being transferred, would create enormous liquidity problems, this lack of liquidity would force the sale of many small businesses to large Canadian or foreign corporations. If the tax system treats a transfer of capital as if it were the earning of income, recipients of such transfers may come to do likewise, and the present view that this capital should be preserved and reinvested may be displaced by a disposition to consume it in the same way as ordinary earned income. The Report has not taken into account the detrimental effect that such a change of attitude would have on private saving. As well, the attempt to tax small gifts and noncash benefits between friends and relatives would destroy taxpayer morale and lead to widespread evasion. An income tax on gratuitous transfers would discourage lifetime giving and would distort testamentary distributions to a much greater extent than does the present system. The proposed devices of block averaging, income adjustment accounts, and registered retirement income plans could not materially alleviate the liquidity problems that would arise. The burden of a simultaneous impact of two taxes would be aggravated by the concept of the family unit, under which dependent children on leaving the family unit would be deemed to receive even their own property as gifts from that family unit. The treatment of gifts as income would also be applied to trusts, posing particular liquidity difficulties for a trustee who must pay an initial tax, often at 50%, on property put into the trust, and distorting the relative interests and rights of beneficiaries of the trust.[14] It would lead to such absurdities as the double taxation of wedding gifts that are received before marriage by a girl who is still a member of her parents' family unit and that are then taken by her into her new family unit—not to mention the valuation difficulties involved. Unlike in the case of the proposal to tax capital gains as income, there would not even be any administrative simplification in taxing gifts, which would still need to be distinguished from other transfers in order to determine whether the proposed annual and lifetime gift exemptions apply.

Indeed, the Report's concession that there should be annual and lifetime gift exemptions is an implicit recognition that gifts are not the same thing as income. Here again the "logic" of the Report prejudices analysis: an equally plausible theoretical argument can be made to exclude from the c.t.b. any transfer that does not represent a component of the national income. The question here is simply not one of theory but one of practical consequences; and the taxing of gratuitous transfers as income would be intolerable. Indeed, with an effective taxation of capital

14. See vol. 4 p. 173.

gains the need for any federal tax on capital transfers is doubtful, since all economlic gain would be taxed once. Accordingy there should be no income taxation of gratuitous transfers, whether made directly or via trusts, and miscellaneous noncommercial benefits should also be excluded from taxation. The provinces should be left with exclusive jurisdiction to impose gift taxes and estate taxes;[15] and there should be an agreement for exchange of information between the federal and provincial taxation authorities to ensure that information obtained by one taxing authority can be used to prevent evasion of the taxes imposed by the other. This step alone would result in an enormous simplification in the Report's proposals and would eliminate numerous objections that have been raised to many aspects of the Report. It would be far preferable to following a suggestion that is frequently made to abandon the deemed realization of appreciated assets—a suggestion that would open the way to substantial tax avoidance. The revenues now collected by the federal government through gift and estate taxes are quite insignificant, so no material sacrifice of existing revenue is involved. If it is not feasible for the federal government to abandon these taxes at once, they should be retained in their present form until they can be left to the provinces as part of a federal-provincial tax arrangement.

Dollar "gains" attributable to inflation are not gains at all and should not be taxed. At the present rate of decline in the purchasing power of the Canadian dollar it would be oppressive to extend the tax base to include all capital gains without permitting an appropriate adjustment for inflation. Indeed the present system already taxes as income certain inflationary gains, but the proposed system would do so on a more extensive scale. Yet the Report dismisses the question of an inflationary adjustment in a few lines of unconvincing rationalization.[16] While it is true that full adjustment for inflationary gains and losses on all transactions would require a substantial revision of present methods of measuring income, a start can be made at least where the impact is most severe. Index numbers could be prescribed by regulation for each year to permit an adjustment of monetary gains and losses on assets held longer than one year. As well, consultations should take place with the Canadian Institute of Chartered Accountants with a view to developing a fully integrated system of adjusting for inflation in the measurement of income.

Life insurance proceeds (except for the investment income component) and compensation received for loss or impairment of earning capacity should be regarded as payment for a loss of capital and should not be treated as income, since the loss of capital cannot otherwise be measured or deducted. The Report grudgingly proposes initially to exclude from the c.t.b. any mortality gains or losses on life insurance, as distinguished from the investment income element, though it contemplates that at a later date these gains and losses might be included. It recommends that any compensation for personal injury to the taxpayer should be included in his income—which could be oppressive in some cases. Instead of providing a general rule, as the Report does, for the deduction of contributions to various compensation funds and for the taxation of all receipts and transfer payments, the tax system should follow a more flexible approach. Such transfer payments as unemployment insurance benefits

15. This is also recommended in the Report of the Ontario Taxation Committee (the "Smith Report"), released in August 1967.
16. See vol. 2 pp. 33-34, 47; vol. 3 p. 349.

and old age pensions are intended to be in lieu of earnings and should be taxed, as should workmen's compensation when received for loss of earnings but not when received for bodily harm or loss of earning power. There should be no need to tax welfare or relief payments.

The Report rightly abandons any attempt to tax imputed income, though the resulting tax base is a much more pragmatic concept than a majority of the Commissioners would care to admit. When gambling gains and losses are in question, however, the moralistic tone returns, and pragmatism and common sense are again abandoned. Apart from the unwillingness to allow the deduction of gambling losses on a basis consistent with the proposed taxation of gambling gains, the whole proposal would create an administrative nightmare and would yield virtually no revenue. Gambling gains and other windfalls should be included in income, and corresponding losses should be deductible, only if they arise as part of carrying on a business; [17] some presumptive rules on a formula basis might be instituted by regulation for determining when gambling amounts to a business and not a mere personal diversion. The Report proposes that there be a $ 25,000 lifetime exemption for gains on residential and farm properties, so as to permit most people to avoid keeping detailed records for this kind of property; but this purpose would not be accomplished, because records must be retained on a lifetime basis, particularly by younger taxpayers, to determine when the exemption is exceeded. The Report is also inconsistent in not allowing deduction or capitalization of the costs of holding non-business property that is later disposed of at a gain. This whole approach would lead to administrative chaos and might reduce the mobility of the population. As already noted, it would greatly aggravate valuation problems at the date of implementation and, indeed thereafter. Yet there does not seem to be much scope for tax avoidance if personal assets are excluded from the purview of the tax system. Accordingly gains on disposals of the owner's personal residence (whether or not associated with a farm) and on other property held for personal use should not be taxed, and corresponding losses should not be deductible; as at present, though, if the property is converted to an income-earning use it should be deemed to have been acquired at a basis equal to its value at that time. Gains on the sale of farm properties (apart from the portion relating to the farmer's own residence) should be taxable in the same way as gains on the sale of any other kind of business property.

The Report concedes that, for the most part, it is impracticable to impose tax on gains until they have been realized, though this concession does further material damage to the "logical" basis of the c.t.b. Again, as a practical matter taxing gains at the time of realization is far more appropriate than atempting to tax increases in the market value of an asset while it is being held. The Report seems often to be obsessed with the dangers of tax deferment, but it does not recognize that normally when tax is deferred because of lack of realization, enjoyment is also deferred and that any ultimate gain from postponement will also be taxed. Where this is not the case a doctrine of deemed realization must be invoked, as the Report recommends in the case of a transfer of appreciated property by gift, on death, on its exchange for other property, presumably on its appropriation for personal use, and at the time the

17. It seems clear that whether or not the Report's proposals are followed here, it will be necessary to determine when gambling amounts to a business, as is the case now.

owner becomes a nonresident. These rules in general seem essential if widespread tax avoidance is not to occur, but they should be accompanied by liberal averaging provisions and probably by more generous rules for postponing payment of the resulting tax than are now contemplated in the Report. With the elimination of assets held for personal use, the exclusion of purely inflationary gains, and the removal of the simultaneous impact of an income tax on the donee of a gift, the rules for deemed realization should be entirely manageable and fair. There will be some inevitable lock-in effect with respect to appreciating property and some tendency toward the early disposal of depreciating property, but this effect should be comparatively moderate and at least as tolerable as under the capital gains taxes of other countries; the lock-in effect is partial only, and seldom can a bad investment be turned into a good one by retaining it to postpone the tax impact on its realization. The proposals that there be a deemed realization on most exchanges of property (as in the case of corporate amalgamations) are insufficiently developed: a general principle should be established that there is a deemed realization only where a readily marketable asset is received in exchange; then more detailed rules can be provided by regulation.

The cost and the administrative difficulties that would be involved in the proposals to permit voluntary revaluations could be enormous. The suggested future system of compulsory revaluation is frightening—an example of the Report's "logic" gone wild. With liberal averaging provisions, it would not be unfair to deny to taxpayers the right to revalue property until it had been realized or a permanent loss in value had been established. The suggestion that when control of the shares of a corporation changes hands its depreciable assets may be revalued is impracticable and should not be followed, particularly in a tax system that recognizes gains and losses on the disposal of shares. Similarly the proposed quick writedown of an investment in new shares of mining and petroleum companies[18] would be administratively complex. These latter suggestions are bound up with the "logic" of the integration system, which I shall later contend should be rejected.

THE FAMILY UNIT

By a somewhat superficial and questionable social analysis, the Report concludes that the family (consisting of husband and wife and dependent children) constitutes the basic social and economic unit in Canadian society and therefore should also be the basic tax unit. In fact if there is a basic economic unit it varies from place to place in Canada and among different social and economic groups. Often the family as defined in the Report is an economic unit for some purposes and not for others: husband and wife may pool some but not all of their property, and children are usually permitted to spend or invest their own earnings. On the other hand, other persons such as dependent parents, siblings, and other relatives are often in fact part of the family economic unit. Thus "logic" and superficial sociology are doubtful guides in determining the basic tax unit. Pragmatically though, it is difficult to achieve a meaningful separation of the respective tax positions of husband and wife; therefore the family unit proposal, insofar as it extends to the spouses, is valid and should be adopted. Children should not be included, because they do not have the same permanence of connection with their parents' economic unit and because of the inevitable confusing and sometimes (even after eliminating the main obstacle of

18. See vol. 4 p. 345.

taxation of gratuitous transfers) oppressive tax consequences on a cessation of dependency. This will avoid taxing children's earnings, which they tend to regard as theirs, at the parents' marginal personal tax rate and taxing the parents on any appreciation in the child's property during dependency. In certain cases an adult taxpayer who has no living spouse or is separated from his spouse should be permitted to claim another dependent adult as part of a family unit. As a result of these suggested changes in the Report's proposals, another look would need to be taken at the relationship between the proposed tax rates for family and for individual tax units.

If gratuitous transfers are not to be taxed, any problems relating to transfers between spouses disappear. Otherwise the Report's proposal that during the first five years of marriage interspouse transfers in excess of one-half of income after tax not be exempt unless and until there is a natural-born (not adopted) child of the marriage, without even a provision for refund after the five-year period ends or when a spouse dies or a child is born within the period, is absurd. It indicates the lengths to which "logic" must go when gifts are to be treated as income. If children are excluded from the family unit there will still need to be provisions to ensure that a parent does not avoid tax on property income by transferring the property to his child[19] though comparable provisions relating to husband-wife transfers and other artificial husband-wife transactions[20] will not be needed. The suggestion in the Report[21] that if a man continues to control the source or disposition of income from property he has transferred he should still be taxed on it, is sound and should be given general application. As long as transfers on death outside the family unit are not subject to income tax, the tendency that would be strongly encouraged by the Report's proposals to leave large amounts of property outright to widows, who would probably not employ it in an enterprising way, would be considerably diminished.

19. See section 22(1) of the Canadian Income Tax Act.
20. See ibid. section 21.
21. Vol. 3 pp. 542-43.

TAX RATES

For revenue reasons, the proposed personal tax rates for family and individual taxpayers would need to be reconsidered in consequence of the net revenue impact of any other modifications made to the Report's proposals. Since the net impact of such changes will probably be a reduction in the revenue anticipated by the Report, personal tax rates as a whole would have to be set at a higher level. This adjustment can be made with fewer qualms once the dogma of discretionary income is discarded. The Commission, in the face of a staff report and the verdict of all studies on the subject to the contrary, asserts in doctrinaire fashion that high personal tax rates materially reduce incentives to work and invest; this conclusion is particularly strange when similar arguments against capital gains taxation are rejected. In recommending that personal rates not exceed 50%, and then only at the $ 100,000 income level, the Commission was probably influenced by the enormous scope of the c.t.b. that it had prescribed. If this scope is reduced, higher personal tax rates become practicable. In any event, political pressures for higher government revenue would tend rapidly to force up the low tax rates proposed in the Report. The Commission departs from its "ideal" rate schedule so as to avoid any material tax reason for the "brain drain" from Canada to the United States; but taxes must be such an insignifi-

cant element in the decision by a Canadian to migrate to the United States that a distortion of the rate schedule for this purpose would be both ineffective and expensive in terms of lost revenue. The Report seems to be on firmer ground in concluding that the personal income-tax burden on middle-income Canadians who do not make substantial capital gains is now too high; this is particularly true of professionals, whose high earnings tend to be concentrated in a limited number of years. A more gradual progression of the rate structure is called for. The marginal personal rates could perhaps reach 50% at a taxable income of about $ 40,000 and 60% for all taxable income over about $ 70,000.

The proposal that there be tax credits rather than deductions for dependents and for working wives is inconsistent with the concept of discretionary income. The Report attempts to justify the tax credits as making the tax system more progressive; but progressiveness is already built into the rate structure. These concessions should take the form of deductions in computing taxable income and should be in line with a reasonable minimal cost of maintaining the dependent, hiring a housekeeper, or whatever the reason for the allowance may be.

The system of block averaging of income over a period of years and of noninterest-bearing income adjustment accounts proposed to cushion the impact of high personal tax rates applied to the annual c.t.b. is inadequate to prevent hardship in many cases.[22] The only justifiable way of combining progressive rates and the c.t.b. is to do so on a lifetime basis—i.e., averaged over the earning lifetime of the personal tax unit. Lifetime cumulative averaging is probably just as feasible as the five-year block averaging proposed in the Report.[23] Each year the computer in the Taxation Data Centre could update the taxpayer's lifetime records and inform him of the cumulative total of income and tax (adjusted to current dollars by the application of prescribed index numbers) and the number of years over which to average his new total. Income adjustment accounts would be superfluous, and the carryover of noncorporate business losses might also be eliminated. There should be generous provisions to permit postponement of the payment of tax on deemed realizations of nonliquid property. If the government wished in any year to enact a special personal tax increase or reduction for purposes of having an immediate impact on economic activity, this might be declared to be exluded from the tax that is to be averaged.

CONCESSIONS AND ALLOWANCES

The proposed $ 500 floor on deductible charitable donations made in a form other than cash, which is recommended for reasons of administrative convenience, would probably have the opposite effect. In any event, it could be circumvented by a simple exchange of cheques. Gifts of property should be

22. The several ad hoc income spreading devices could act quite unevenly. The disallowance of interest on income adjustment accounts (i.e., tax-deferred deposits with the government, subject to several restrictions) would be punitive in an inflationary economy; and these accounts would only be useful when the taxpayer had liquid funds to place on deposit—when tax deferral is least needed. It is also harsh to require all such accounts to be liquidated when the taxpayer reaches the age of 60.

23. The Report would give taxpayers the option to average their income over fewer than five years, but this would force the taxpayer to gamble whether to wait until the end of the five-year period or to average sooner.

valued and should be decuctible on the same basis as gifts of cash. If the gift is of property held for income-earning purposes there would be a deemed realization at fair market value, but this should not prejudice the donor, because if the $ 500 floor is removed his charitable deduction would be at least as large. The suggested 10% limit on deductible corporate charitable donations as against a 15% limit on individual donations is an example of where the Report negates the "intermediary" view that is at the basis of its integration proposals. With appropriate control over the financial reports of charitable institutions and over their procedures for issuing donations receipts, which is now being instituted, there may be no valid reason for placing an annual limit on deductible inter vivos donations under a system of lifetime cumulative averaging. As a minimum, there should be an indefinite carryover of undeducted donations.

The Report's proposals relating to registered retirement income plans are unsatisfactory, though they have the virtue of recommending consistent treatment for pensions and other types of deferred income plans. The proposed limit of a paid-up $ 12,000-per-annum pension is too low, particularly for younger contributors in an inflationary economy. Any figure that is chosen in this way would encounter the administrative problems of coordinating several different plans covering the same individual, of attributing the earnings of overfunded plans, of dealing with unvested contributions, and of applying the rules to foreign pension plans. The only practicable solution seems to be to limit deductible contributions to a percentage of earnings and to allow past-service contributions to pension plans on a formula basis along the lines of present administrative practice.

CORPORATE TAXATION AND THE INTEGRATION PROPOSAL

The proposal to eliminate the low rate of tax on the first $ 35,000 of taxable corporate income is sound and should be adopted, regardless of the disposition of the integration proposals. The present dual rate structure is costly in terms of lost revenue, creates numerous problems of tax avoidance, and—provided that, as the Report suggests, small closely held corporations are permitted to pay tax on a partnership basis—is not needed as a concession to small business.

The integration proposals are among the least satisfactory aspects of the Report. Most corporate income in Canada is earned by large corporations, whose shares directly or indirectly are widely held; these corporations are separate decision-making and taxpaying units, with a management wholly or largely independent of the ultimate shareholders and with none of the economic attributes of an intermediary, and they shift corporate income taxes to a substantial though indeterminate extent. The Report chooses the closely held corporation as the norm and contemplates that integration would result in "reverse shifting", which would turn all corporations into intermediaries. This will not occur in widely held corporations, partly because integration would not remove the independent decision-making position of their management; partly because many of them are controlled by nonresidents, who will not benefit from integration; and partly because a separate corporation income tax is built into the price system of this country and also of its neighbors and competitors. The Report seems to assume that the closely held corporations, rather than the widely held corporations, will set market prices; this is unrealistic. While the Report claims that it is not assuming nonshifting of the cor-

porate income tax, in fact it does: in most of its tables comparing the total tax borne by individual shareholders now and under the proposed system, nonshifting is consistently assumed.[24] The suggestion that integration would lead to significantly higher purchases of shares by lower-income taxpayers is unconvincing: the absolute tax benefit in relation to the small investment that could be made would not materially affect established patterns of spending and saving among these groups.

Those who owned shares in widely held corporations at the time of implementation would reap windfalls from the enhancement of share prices that would result from integration; the Report deplores this but accepts it as a necessary price for rationalizing the tax system. To the extent that reverse shifting does not occur, subsequent, shareholders would receive further windfall benefits. The uncertainties resulting from integration, with its unequal treatment of resident and nonresident shareholders, may be expected to cause fluctuations in share prices and perhaps large movements of foreign exchange, adding more elements of instability to the market. The idea of refunding to a shareholder a tax that he has not paid and has not borne is repugnant; even if such a system were initially instituted, it could not survive political pressures for change. As well, the record-keeping requirements that would be imposed by integration would be extremely burdensome. In summary, integration should not be adopted; corporations should be taxed at about 50% on all taxable income, but closely held corporations—within more generous limits than suggested by the Report—should be permitted to elect to be taxed on the same basis as a partnership. The averaging of corporate income over a period of years would be unnecessary and probably undesirable; but a carryover of annual corporate losses, along the lines suggested by the Report, should be permitted.

Since complete neutrality between taxation of corporate-source income and of other income is not attainable, departures from the present pattern of taxing corporate-source income, which is built into the economy, should not be made lightly, and probably any transition should be gradual. Unfortunately the need to abandon integration will require a reconsideration of the problems of corporate surplus and of taxation of dividends and share gains, since the Report gives little attention to alternatives to integration. It is also vague and unhelpful on the treatment of corporate surplus on hand at the date of implementation, some of which would have borne corporate tax only at the low rate of 21% or 23%. The Report perhaps unduly disparages the recommendations of the "Committee of Four" that all corporate distributions bear a flat rate of tax of 15%, with no further tax in the hands of the shareholders but allowing some refunds to low-income shareholders;[25] if this recommendation were combined with the taxation of share gains a procedure for "allocation" of corporate surplus to shareholders, somewhat along the lines proposed in the Report as part of the integration procedure, would be desirable; there would be attendant record-keeping difficulties, though not of the same magnitude as under integration. The proposed flat rate of 15%, if part of a system that permits partnership treatment of small closely held corporations, seems too low, however.

Perhaps a better alternative would be to

24. On the other hand, the Report sometimes reverts to a "separate entity" view—e.g., in the limits imposed on deductible charitable donations and in not permitting the corporation to deduct the cost of granting stock options.

25. See the discussion at vol. 4 pp. 37-44.

continue the present flat-rate credit against the tax otherwise payable by a resident individual who receives dividends from taxable Canadian corporations. This credit is now 20% of the dividend, and while the Report asserts that it discriminates against the lower-income shareholder, most of this "discrimination" arises from the fallacious assumption that the corporate income tax is not now shifted. In fact, with the tax credit often having the effect of reducing the tax on other income, the lower-income shareholder finds this tax concession very attractive. Subject to revenue requirements, the tax credit might be raised to 25%, so that the highest personal tax that could be paid by a resident individual on a dividend from a Canadian corporation might be about 35%—which would recognize that the corporate income tax is partly shifted. The same credit should be granted against gains on sale of shares, so as not to discriminate between corporate distributions and retentions of surplus. Under such a scheme it would be necessary to prevent individuals from selling the shares of a corporation that holds appreciated property in lieu of selling the property, and so considerably reducing the burden of taxation. If the shares are acquired by other taxable residents the tax burden would presumably be adjusted through the price; but there might have to be some antiavoidance provisions for closely held corporations—perhaps requiring partnership treatment in certain circumstances. In any event, this difficulty would be far simpler to deal with than the existing problems of "surplus stripping", which would disappear with the taxation of share gains. All "gifts" by corporations, as now, should be treated as either dividends or salaries. Intercorporate dividends would be tax-free, except that when such dividends are paid out of preacquisition surplus they would reduce the basis of the shares.[26]

EMPLOYMENT INCOME

In seeking to tax small noncash fringe benefits conferred upon employees, the Report's consistency and "logic" are again at odds with practicability and common sense. There is now a fairly reasonable administrative accommodation in this area, under which materiality is the prime criterion. This general approach should continue, though the lists of items taxed and not taxed might be re-examined; and the rules from time to time in effect should be formally embodied in regulations. The assumption in the Report that the recipient of a noncash benefit had the choice of taking its market price in cash is both unrealistic and unfair; tax should be based on the benefit to the employee (if material) and not on the cost to the employer or a national market price. Stock options should probably be taxed on the value of the shares at the time the option is conferred rather than their value when the option is exercised. The proposed treatment of group life insurance, allowing deduction of premiums and taxing the proceeds as income, is probably undesirable: to be consistent with the treatment of other types of life insurance not in a registered retirement income plan, the premiums paid by the employer should be taxed to the employee, and the proceeds of the policy should not be taxed; the employee would still benefit from the favorable group rate and from his employer's payment of the premiums. Strike pay and similar benefits from union and professional organizations should be taxable, as proposed, and annual dues to these organizations should be deductible, as now.

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26. The "personal corporation" rules, relating to family-held investment companies, could be simplified into a mandatory partnership treatment in certain cases.

The recommendation that the actual expenses of earning employment income be deductible is valid and would remove a serious inequity in the present system, though at the cost of some administrative inconvenience. Yet the alternative of an optional deduction for all employees of 3% of income (maximum $ 500) is indefensible, even if it slightly reduces the administrative problem: most employees would have actual expenses far below that level, and probably an optional deduction of $ 50 in addition to actual union and professional dues would be ample.

BUSINESS INCOME

In general the Report makes some useful proposals on the measurement of business income, particularly in recommending that certain artificial existing rules be eliminated. Unfortunately the Report relies too readily on the conclusion of a committee of the Canadian Institute of Chartered Accountants that there should be no specific reference in the law to accounting principles or practices as the starting point for measuring income for tax purposes. Even in the absence of such a reference the courts will normally look to accounting practice, but to the extent that they do not, the law will be erratic and unpredictable. The dangers of rigidity feared by the committee could be avoided by appropriate drafting.[27] The recommendations for more extensive use of the accrual method of accounting seem sound, though some concessions may have to be made on the timing of payment of tax for a professional practice or business that cannot readily borrow funds on the security of its accounts receivable. The Report's bias against inflationary adjustments appears again in the artificial restrictions that it proposes on the use of the last in first-out (LIFO) method of inventory accounting; this method should be available whenever it is appropriate as a matter of accounting practice.

On the deduction side, the Report again makes a useful contribution by recommending the deductibility of all expenses reasonably related to the earning of income, providing they are not unreasonable in amount or of a personal nature, and by recommending that all "capital" or deferred expenses that are of a deductible kind and amount be deductible at some point of time. This approach would remove most of the difficulties and inequities that have grown into the present system.[28] The proposed restrictions on travel and entertainment expenses, however, are objectionable in both amount and principle. The evidence revealed by a official study of the problem indicates that there has been little abuse in this area that cannot be remedied by existing administrative procedures, and consequently the harsh and arbitrary limits proposed by the Report are unjustified. The same tests of reasonableness in relation to the earning of income should apply here as elsewhere, though it might be useful to have guidelines issued by regulation as to what is prima facie unreasonable, having some regard to the time, place, and circumstances.

The recommendation that the existing basic system of depreciation[29] be continued is sound, even if it results in some discrimination in favor of capital-intensive activity. The suggestion that depreciation should not be deductible until the asset is put into use, however, is neither practicable nor desirable: it is much easier to determine when an asset

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27. I have discussed this matter at greater length in Can. Tax Foundation, Proceedings 19th Tax Conf. 93-98 (1967).

28. See my further discussion ibid. at 98-101.

29. This for the most part is on a diminishing-balance basis. It is often referred to by the technical name "capital cost allowance".

is acquired[30] than when it is put into use, and in any event the rates and methods for computing depreciation are arbitrary and are made generous so as to encourage capital investment. The proposed rapid writeoff incentive for small business should not be enacted: it is an incentive of limited value, and it would lead to enormous administrative and tax-avoidance problems.[31] Small closely held corporations would have the option to pay tax on a partnership basis, so that the tax system would not discriminate against them; beyond that, the tax system is not an efficient means of providing incentives for small business.

The arbitrary rules proposed for distinguishing personal from business losses are unsatisfactory and would lead to much administrative complexity, particularly in having to distinghuish one business from another. Instead of arbitrary rules, such as whether losses have been sustained in three years out of five, the general principles proposed for expense deductibility should apply.[32] Similarly the proposed restrictions on the deduction and carryover of losses from holding property for other than personal use[33] are unnecessary; these should be treated in the same way as business losses. As recommended earlier, gains and losses on assets held for personal use should not enter into the tax base. The privilege of filing consolidated returns should not be confined, as the Report suggests, to wholly owned affiliated companies.

One of the most controversial aspects of the Report has been its recommendations to remove the existing tax discrimination in favor of mining and petroleum companies. It was to be expected that those who benefit from such discrimination would protest bitterly that the health of the Canadian economy depended on the continuation of these tax advantages; and they have been able to win some converts. Actually almost every argument that has been raised was anticipated and disposed of in the Report and its supporting studies. Tax concessions to extractive industries are an inefficient incentive for accomplishing any legitimate social or economic purpose, as the Report carefully points out. There is no question that, other things being equal, a withdrawal of these enormous tax concessions would reduce investment in these industries, but it would also permit greater investment in other industries that are more efficient. The fact that a particular marginal mine would not have been developed without these concessions is not a convincing argument. If there are justifiable economic, social, or even military reasons for developing a particular region or industry to a greater extent than would occur under a tax system that is neutral as between industries, this should be done in the open by a system of subsidies, which can be confined to cases where they are needed. The only argument of any substance that seems to have been raised against the Report's recommendations is that some other countries offer tax incentives to extractive industries and that capital that otherwise would be invested in Canada would be attracted instead to one of these other countries. This argument, however, seems to overstate the case; at best it is comparable to the argument that Canada should have at least as high a tariff level as its most protectionist competitor. While no valid case seems to have been made for continued tax favoritism to these industries, it is essential that an appropriate subsidy system

30. Even here, however, the present Act and Regulations are hopelessly obscure and incomplete.

31. See, e.g., Townsend, in Can. Tax Foundation, Proceedings 19th Tax Conf. 88-91 (1967).

32. See my discussion ibid. at 102-03.

33. See vol. 3 pp. 108-09.

be instituted and that existing incentives be withdrawn on a very gradual basis, so as to cushion the impact of the change. On the whole, the Report recognizes this need. The result in terms of the net effect on government revenues, however, is bound to be much less impressive than the Report anticipates. The Report rightly recommends a rapid writeoff of exploration and development expenses in these industries; but administrative complexities[34] and the abandonment of integration would militate against the proposed quick writedown of an investment in new shares of an extraction company. The recommendation that provincial mining and logging taxes be treated as a deduction rather than a tax credit seems sound, because these are basically inventory costs rather than income taxes.

On the whole, the recommendations for taxing financial institutions seem sound, though issue might be taken with some of the details. Thus, the recommended allowance for bank bad debt losses may be somewhat too low. The proposed full taxation of life insurance companies seems to be necessary to eliminate a serious discrimination in the existing system, even though it would increase life insurance premiums; but the proposed 20% tax to be paid by the insurer on its reserves for term life policies should not be applied to existing policies. The recommended arbitrary allowances for loss on mortgage investments over and not over 75% of the value of the property may create some administrative difficulties.

The Report correctly concludes that cooperative enterprise has been unduly favored by the present tax system, but its proposed solution amounts to an overcorrection, which would tax imputed income. The fact that members of a consumer cooperative may be able to buy goods more cheaply than other consumers is not conclusive that they should be taxed on the difference, unless *all* imputed income is to be taxed. The proposed solution would encourage "pricing out" by cooperatives, which is financially risky and may be destructive of cooperative principles. The Report admits [35] that there are other loopholes in its proposals, which would make it possible to convert cooperative investment income into imputed income. Here again, only approximate equity and neutrality can be expected from the tax system. Producers' cooperatives should probably be taxed at 50% of their investment income and of net other earnings after deducting patronage dividends (but patronage dividends should be deductible only to the extent that half of them are paid in cash), as recommended in the Report; distributions of income that has been taxed to the cooperative should be treated in the same way as corporate dividends. Consumer's cooperatives should pay tax at 50% on investment income and income from business with nonmembers, and distributions from these sources should be taxed as corporate dividends. Otherwise members should be taxed on patronage dividends, as at present, only if these are not related to consumer goods or services. For this purpose, credit unions and mutual insurance companies should be taxed on the same basis as cooperatives. No other tax concessions should be given to cooperatives. These recommendations should remove any significant tax advantage now enjoyed by cooperatives without penalizing imputed income because it is received through a cooperative; cooperatives would continue to be recognized as intermediaries to the extent that they genuinely act as agents for their members.

34. See vol. 4 p. 345.
35. Vol. 4 p. 107.

PROPERTY INCOME

It would be unfair to follow the proposal to tax all dividends on life insurance policies as income to the policyholders. The Report admits that this approach would be arbitrary but is unable to suggest a better one.[36] Just as in the case of consumer cooperatives, the dividend represents in part a refund of the recipient's original contribution to the corporation, in this case the policy premium. To the extent of the difference between the premiums for a participating and a nonparticipating policy of the kind in question, policy dividends should be deductible to the insurance company but should only be taxable to the policyholder if the premiums were deductible. Policy dividends in excess of this difference should be treated in the same way as corporate dividends.

The Report's prediction that its proposals on taxation of trusts would eliminate the income tax advantage from the accumulation of income is overoptimistic.[37] In the taxation of trusts, as in so many other aspects of the Report, the record-keeping implications of Report's proposals are staggering, and the analysis of the problem in the Report is incomplete. If the taxation of gratuitous transfers is eliminated, however, the rest of the trust recommendations become reasonable. In particular, the option now available in certain cases to treat the trust as a separate individual taxpayer should be eliminated, and trust income should be taxed on the basis that the trust is an intermediary for its beneficiaries.

INTERNATIONAL TRANSACTIONS

Most of the proposals for changing the present system of taxing international transactions seem to be unsound or questionable. The analysis in this part of the Report is almost consistently unconvincing, and most observers agree that these proposals, if implemented, would have a harmful effect on the Canadian economy. Here, particularly, the incompleteness and obscurity of the recommendations in some vital aspects are remarkable.[38] The Report correctly concludes that section 28 (1) (d) of the Canadian Income Tax Act, which exempts dividends received by a Canadian corporation on a direct investment in a foreign corporation,[39] has permitted tax avoidance and should be withdrawn. At the same time it seems unfair to tax, on an accrual basis up to a level of 30%, income from business ventures by Canadians in countries having a low rate of corporate tax, when competitors from other countries are not so taxed; it is different if a tax haven is used solely as a base for operations in third countries. At the other extreme, limiting the foreign tax credit to 30% is an unjustifiable discrimination against foreign investment by Canadians: as a matter of comity as well as fairness, there should be a

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36. Vol. 4 p. 411.

37. See, e.g., Goodman, Estate Planning and the Royal Commission Proposals, 15 Can. Tax J. 303 (1967), and panel on Estates and Trusts, in Can. Tax Foundation, Proceedings 19th Tax Conf. 367 (1967).

38. For example, the manner in which the additional 20% tax on foreign-source income of Canadian corporations is to be paid when this income is allocated to Canadian shareholders; the treatment of losses on foreign investment; the adjustment of the basis of shares in direct-investment foreign corporations to account for the accrual of foreign income; and the offsetting of earnings on foreign direct investment against Canadian losses.

39. In section 28(1)(d) the criterion of directness is the holding of more than 25% of the voting shares; the criterion proposed by the Report is an interest of 10% or greater.

full credit for foreign taxes up to the total Canadian tax on the foreign income. The proposed 30% limit would not only be discriminatory but would also render difficult or impossible the continued operation in Canada of the headquarters of several large international corporations. As a result of combining the proposals for taxing foreign income with the integration system, after all the complex computations and allocations have been made Canada may have to refund to a Canadian shareholder some of the foreign tax that has been paid.[40] Once again, administrative detail and record-keeping obligations would be onerous, particularly in the attempt to measure foreign income by Canadian standards.

Probably the only feasible solution is to avoid the attempt to accrue the recognition of foreign income earned through a foreign corporation, unless it can be shown that the foreign corporation had no business purpose other than to avoid or postpone Canadian tax. When the foreign income is remitted to Canada in the form of dividends on the direct foreign investment, the dividend should be grossed up to its before-tax level (as earned by the direct-investment corporation and its first level of subsidiaries), and credit should be given for the total foreign corporate and withholding tax up to the amount of Canadian tax on the grossed-up income; this computation should be done on a per-country basis, with a right to carry forward unused foreign tax credits relating to any country. Section 28 (1) (d) would be eliminated and would have been replaced by a more sophisticated but not too burdensome system.

As mentioned earlier, the Report contemplates a harsher Canadian tax treatment of nonresident income from Canadian sources. Most of the recommended changes to the present system seem to be unsatisfactory. The proposed 30% withholding tax on interest, salary, and other nondividend payments would not have wide application, because it would be overridden by many existing tax treaties; but wherever it applied it could be oppressive. The proposal to treat interest paid to a nonresident affiliate as a dividend would also be harsh and unfair, particularly with respect to existing arrangements; the only time that such a rule should apply is where the nonresident recipient is established in a tax haven and therefore does not pay significant income tax on the interest; in that case Canadian tax might be imposed at such a rate that, when it is combined with any foreign tax that the nonresident must pay on the interest, the total tax is 50%. Canadian taxation of gains by nonresidents on the disposal of property in Canada should not be limited, as proposed for administrative reasons, to nonresidents having a permanent establishment in Canada: collection difficulties in some such cases should not affect the principle that income has been received from Canadian sources and is properly subject to a Canadian withholding tax. On the death of a nonresident who owns property in Canada there should be a deemed realization of that property. Except for Canadian subsidiaries of foreign enterprises that changed their position in response to the low 10% withholding tax on dividends to nonresidents granted a few years ago to corporations that have "a degree of Canadian ownership", the dividend withholding rate for all corporations, as the Report recommends, should be restored to 15%. Even the few corporations that did take steps to qualify should not have the benefit in perpetuity: the privilege should be continued for perhaps five years after the normal rate returns to 15%.

A particularly troublesome feature of the international proposals in the Report is the

40. See Table 26-1, vol. 4 p. 519.

required valuation of all property owned by a person who assumes or relinquishes Canadian residence and the deemed realization of all property when the owner becomes nonresident. If no modifications in this practice are made, it might become hazardous for anyone to take up temporary residence in Canada. The movement of personnel to and from Canada would be checked and perhaps stopped. Accordingly there should be special provisions for persons who are temporarily resident in Canada and who do not during their period of residence realize property owned by them at the time of becoming resident: there should be no deemed realization of such property on the resumption of nonresident status.

The proposed 10% tax on services rendered abroad that are paid for by tax-deductible remittances from Canada, which would not qualify for a foreign tax credit abroad, is also objectionable. This tax would not be an income tax but rather a hidden tariff on services and as such has no place in an income tax system. The existing provisions in the Income Tax Act[41] that impose a 15% tax on certain management fees paid to nonresidents are not mentioned in the Report; if they are to be retained at all, they should be clarified and narrowed in scope. The proposed repeal of the exemption from Canadian tax, on a reciprocal basis, of income earned in Canada by nonresident owners of ships and aircraft would harm existing arrangements and would be too great a departure from prevailing international practice; this change should not be enacted at the present time.

FEDERAL SALES TAXES

Both the political and the transitional problems of giving effect to the proposal to substitute a federal retail sales tax for the present manufacturer's sales tax render the proposal impracticable, even though the Report correctly points out the shortcomings of the present tax. The degree of coordination with the provinces that would be necessary in order to have a common tax base across Canada for retail sales taxes levied by the federal government and now levied by nine out of ten provincial governments is unattainable in the existing state of federal-provincial relations; even if attained, it would remain vulnerable to disruption at any time. As well, the transitional problems of shifting the level of the tax are substantial. The retail sales tax of 15% or higher that would result from combining the proposed federal tax with the existing provincial taxes would create substantial compliance problems and also much annoyance among consumers, particularly if the tax is levied in "direct" form and the quoted price of goods and services is significantly less than what consumers must actually pay. The Report correctly concludes that a value-added tax would involve too much additional record keeping and administration and, because of the high level of tax compliance, is not needed in Canada. The suggestion to include certain services in the sales tax base is sound and will likely be followed by the provinces.[42]

In the circumstances, the most practical approach is for the federal government to retain the present manufacturer's sales tax (though much of the present "unwritten law" should be incorporated into the Act or regulations) and to negotiate the withdrawal of this tax as part of an overall federal-provincial tax settlement. This would permit the provinces to raise the level of their retail

41. Sections 106(1)(a) and 106(1c).
42. The Smith Report, note 15 supra, recommends that the Ontario retail sales tax be extended to certain services.

sales taxes without increasing the total cost to the consumer. While ultimately the federal government should thus withdraw from sales taxation, for revenue purposes (as the Report suggests) it will probably be necessary to retain the existing excise duties and the special excises on wines and tobacco; the other excise duties and taxes, however, should be removed. To simplify the task of the provinces there should be a constitutional amendment, as the Report recommends, permitting the provinces to impose retail sales taxes in "indirect" form.

FEDERAL-PROVINCIAL RELATIONS

The problem of achieving a close cooperation of the provincial and federal governments on fiscal matters has already been raised in the discussion of sales taxation. The unlikelihood of unreserved and continuing federal-provincial cooperation is another reason why the integration proposals would not work, since the Report admits that integration requires that provincial income taxes move only within a narrow range. Some of the provinces, at least, will not accept such a limitation on their taxing powers. While permitting all sales tax revenues to go into provincial treasuries would help provincial finances, the provinces will not be content to abandon income taxes: the Report itself treats sales tax as an inferior kind of tax, which should gradually decline in importance, and sales taxes are not nearly as responsive to economic growth as are income taxes. The provinces require a source of revenue that will grow at least as fast as the economy and preferably faster, since provincial and municipal expenditures are rising at a faster rate than federal expenditures and will probably continue to do so for some time. In addition, strong pressures in some provinces for greater provincial autonomy will lead their governments to reject any form of cooperation with the federal government that would deprive them of a substantial measure of control over the growth of their provincial economies. The suggestion that the federal government can induce the provinces to restrain their expenditures during inflationary periods (i.e. always) by depositing funds in Ottawa in exchange for a bonus appears visionary.

TAX FORMATION, ADMINISTRATION, AND ADJUDICATION

Unfortunately the Report provides virtually no directions for changing the Income Tax Act to improve the quality of judicial interpretation, except for a vague reference to the desirability of using more general statutory language. All tax practitioners know that the Act is badly in need of improved drafting in virtually all of its sections, yet on this question that is so important to accountants and lawyers the Report offers virtually no assistance. The suggestions that there be greater parliamentary scrutiny of proposed tax legislation, however, are sound and should be implemented. As well, the suggestions that there be greater use of public hearings, regulations, and advance rulings should be followed.

The administrative difficulties that would be created by the implementation of many aspects of the Report have already been noted. Most of these would be eliminated or reduced to manageable proportions by some of the modifications to the proposed system that have been suggested here. Certainly an expansion in the staff of the tax administration would be required under any meaningful improvement of the present tax system, but this expansion should be kept within bounds. The Report recommends that, to unify administration and to avoid

both the substance and the appearance of political influence, the tax administration should be given to a semi-independent body known as the Board of Revenue Commissioners. This fear of political influence seems to be exaggerated, and the virtues of removing tax administration from a government department are probably overstated. In any event, these recommendations should not be acted on until after the effects of recent reforms in the tax administration can be evaluated and the disruptions resulting from reform of the tax system have been overcome. The suggestions that regional taxation offices be established and that a series of formal conferences be prescribed in cases of disputes with taxpayers are valuable, however, and should be put into effect at an early date. Similarly, as the Report recommends, greater legal safeguards on searches and seizures by the tax authorities should be instituted.

The burdens of record keeping that the Report's proposals would impose on taxpayers have also been referred to several times. These too should be considerably reduced by the recommended departures from the Carter system, but even so there will inevitably be increased requirements for record keeping by some taxpayers in any improved tax system, particularly one that taxes capital gains. On the other hand, more sophisticated means of keeping records are available to most taxpayers, either directly or through their employers; through corporations, trusts, pension plans, etc. in which they have invested; and through information maintained at the Taxation Data Centre. On the whole, the costs and difficulties of compliance should remain quite manageable as long as the more extreme aspects of the Report are discarded. There will still be compliance difficulties, as now, but the administration today displays remarkable efficiency in finding cases of noncompliance. There is a somewhat cavalier treatment in the Report of the subject of penalties and sanctions for noncompliance;[43] this whole area deserves much more thorough study. Instead of recommending only restricted relief in a limited class of cases, it is surprising that the Report did not recommend that if the tax administration appeals a decision of a tax tribunal, the administration should prima facie be required to pay the costs of the taxpayer, win or lose. It is unfair under the present system that a taxpayer who has won his case before the Tax Appeal Board max find that, though only a small amount of tax is involved, the Taxation Division feels that the case would set an undesirable precedent and therefore appeals to the higher courts, where if the taxpayer loses he must pay his own and the Division's costs. The Report rightly recommends that the wasteful procedure of having a trial de novo in the Exchequer Court when an appeal is taken from a decision of the tax court be eliminated and that appeals to the Exchequer Court should be on questions of law only. The recommended Tax Court, having the prestige and status of a court rather than of an administrative board, should be instituted.

To promote the kind of improved judicial interpretation that the Commissioners want, they might have recommended that the aspects of the Report that are put into effect, the government's White Paper indicating its reaction to the Report, and annual budget speeches explaining tax changes should be admissible in evidence on the question of the purpose of a statutory provision or regulation. In this way the courts would be directed to remove their self-imposed blinkers, which lead to erratic and mechanical interpretation. As well, the courts might be specifically

43. Vol. 5 pp. 151 and 153.

instructed to interpret the tax law in accordance with its apparent purpose, and the doctrine of literal and mechanical construction should be expressly abolished. Finally, a business-purpose test might be instituted by statute to permit the courts through interpretation to thwart the more flagrant cases of tax avoidance.

There should be some permanent administrative machinery for continuing research on tax law and administration, which would make recommendations for improvement on an integrated and ongoing rather than piecemeal basis. This group of experts would presumably keep under continuous study the essential and practical kind of tax problems that the Report so often ignores.

CONCLUSION

In view of the cost of preparing the Report, the longterm suspension of constructive improvement in Canadian federal tax law during and since the Commission's deliberations, and the disappointing and incomplete results, it may be questioned whether a royal commission is a suitable device for attempting to improve the tax system. Perhaps the idea of a permanent group of experts, just suggested, will be more fruitful. The general reaction to the Commission's more radical proposals indicates that Canadians will sooner support an evolutionary than a revolutionary approach to tax change.

The government's refusal over some years to attempt to improve the existing system while taking refuge in the prospect of a complete solution from the Commission now appears, more than ever, to have been unjustified. The same problems must still be faced, and they seem hardly less difficult now that the Commission has spoken. It may be hoped, however, that the Report has at least narrowed the available alternatives, though on many key questions the Report's proposed solution should not be adopted. The question now is whether some of the insights and ideas in the Report can be used as a basis for adapting and adjusting its recommendations into a viable tax system—even though that system must be somewhat less exciting and "logical" than the Carter vision.

MICHAEL CONNOR, M. COMM.:

INVESTMENT IN IRELAND—RELATIVE FACTORS INCLUDING AVAILABLE INDUCEMENTS AND FAVOURABLE ASPECTS

In dealing with Ireland as a whole the author had same problem (arising from the political division of the country) as he had in preparing his national paper "Outside Industrial Investment in Developing Countries" for the recent Ninth International Congress of Accountants. As in his treatment of his subject in that paper the following article will deal firstly with the Republic of Ireland (26 countries) and then with Northern Ireland (6 countries).

REPUBLIC OF IRELAND

HISTORICAL NOTE

When Ireland became self-governing, just over forty years ago, the country was industrially very under-developed, except for one or two outstanding industries which had become famous over the centuries and are still world-famous today. Whilst recognising that agriculture must continue to play a leading role, the Government, in order to create a balanced economy, set out to build up the industrial side as well. In the early years, its chief task was to create conditions in which industry could develop, and the growth of industry was therefore slow during the first ten years. From the early 1930s onwards development proceeded at a much faster rate.

The lack of an industrial tradition, and the economic conditions in the world as a whole, made Irish investors at first hesitant to invest in new industry in Ireland. They had been too long accustomed to investing in established companies, mainly in Britain. The Government made investment in Irish industry attractive by adopting a policy of protection against external competition, and by introducing new laws which prevented big outside firms from setting up Irish branches and thereby injuring the new native industries while they were still in their infancy. Firms from abroad were, of course, welcomed where they produced goods not already made in Ireland.

The purpose of both these forms of protection had largely been attained by the 1950s. There is now a very substantial Irish investment in industry, and broadly speaking, almost everything needed for the Irish market is made in Ireland. Accordingly, in 1958 an Act was passed, one of the main provisions of which enables firms from other countries to manufacture in Ireland without restriction if their primary object is export. A great many industries established in recent years are in fact 100% owned by outside interests. The Government have recently announced their intention of removing even this last restriction on investment by firms from abroad in industry in Ireland; it will be removed with effect from 1st January 1968.

Although so much has been done to build up industry in Ireland, it is still a major part of the Government's policy to encourage the establishment of many more industries.

GOVERNMENT POLICY

Under the Irish Constitution private enterprise is favoured by the Government. The State has taken an active part in industry only where some particular service was necessary for the economy as a whole (e.g. electricity) and where private enterprise has been unable or unwilling to provide it. Irish businessmen are guaranteed against expropriation. A treaty of Friendship, Commerce and Navigation concluded with the United States of America gives the same guarantees to citizens of the United States as to Irish citizens.

The first objective of Government policy is the creation of new jobs to absorb workers leaving agriculture because of increased mechanisation, and to stem emigration. The method used to achieve this is the development of manufacturing industry and one of the main ways of securing increased industrial development is the attraction of industrial firms from other countries.

A preface to a Government brochure states:-

"This small but advantageously located country offers outstanding attractions to new industry. These include substantial non-repayable cash grants for factory buildings and machinery and training of workers, tax relief on export profits, and a surplus of intelligent and adaptable labour."

"Ireland is well situated geopraphically to serve the major European and North American markets. There are frequent sailings from Irish ports to Great Britain, Europe and North America. Daily air services link Dublin, Shannon and Cork airports with all the main industrial and commercial centres in Great Britain, Europe and America. There is an exellent internal transport system."

1. The Government's Second Programme for Economic Expansion which covers the period 1964-1970 inclusive envisages a 35% increase in real gross national produce (G.N.P.) requiring an annual average growth rate of 4.3% per annum. Industry, especially manufacturing industry is expected to be the main agent of economic growth—an annual average growth rate of 8.2% is envisaged for this sector of industry. It is anticipated that new industries having a gross output in 1970 of £60 millions at 1960 prices will be established during the period 1964/1970—over 85% of this projected output is expected to be exported.

2. GENERAL

Since the commencement in 1959 of the Government's Programmes for Economic Expansion, the volume of output of manufacturing industries in Ireland has grown at an annual average rate of 6.4%; employment afforded by these industries increased from 142,000 in 1959 to 175,000 in 1966 and industrial exports from the 1958 level of £33 millior to £124 million for 1966.

3. The achievements of the industrial sector of the economy are further evidenced by the following statistics. In the eight years 1959-66 new industrial enterprises were set up having an estimated capital investment of £83 million and an employment potential of 40,000. Enterprises with foreign participation numbered 229 accounting for about 80% of the estimated capital investment and employment potential. Of the 229 enterprises with foreign participation over 40% were established by British firms, 20% by Germans, 16% American, 5% Dutch and the remainder by firms of various nationalities including Italian, French, Belgian, Swiss, Danish, South African, Canadian, Finnish, Austrian and Monagasque. Almost all the new enterprises set up by external industrialists are

export orientated, a factor which is reflected in the rise in industrial exports in recent years as is apparent from paragraph 2 above.

Fifty-four new industrial enterprises were established in 1966 of which forty had foreign participation and accounted for about 90% of the estimated capital investment of £8.9m. and 95% of the employment potential of 4,500. In addition at the end of 1966, there were thirty-five new projects under construction of which twenty-nine had foreign participation and which accounted for the bulk of the total capital investment of £11.7m. and the expected employment of 2,800 at full production.

This progress on the industrial front is encouraging and augurs well for the future. It is recognised that industry will continue to play a major role in the development of the economy and the heavy outflow of people from agriculture makes it all the more necessary for the implementation of an intensive industrialisation programme. Measures have been and are being taken to intensify the industrial promotion campaign.

4. This industrial expansion has been mainly due to the Government's policy of providing incentives aimed at the establishment of factories to cater primarily for export markets. Among the bodies implementing this policy is the Industrial Development Authority which is responsible directly to the Minister for Industry and Commerce. The Authority is specifically charged with the task of assisting industrialists who may be interested in establishing manufacturing undertakings in this country.

Such assistance includes collecting and investigating the facts about Irish conditions and in advising how to obtain the maximum incentive benefits provided by the Government for new industries.

GRANTS AND LOAN CAPITAL FOR INDUSTRY

5. Non-repayable cash grants for industrial development are administered by An Foras Tionscal (The Grants Board)—an autonomous body. It examines all applications for grants and works in close liaison with the Industrial Development Authority which assists industrialists in preparing their grant applications. The scale of grants available for new industrial projects in the Undeveloped Areas (the West, North-West and South-West parts of the country) is higher than that for the rest of the country.

Details of grants approved for new projects, capital expenditure and employment potential of these projects are set out below for the period up to 31st March 1967.

	£m
(a) Grants approved for—	
(i) The Undeveloped Areas	11.432
(ii) The rest of the country	15.475
Total—	26.907
(b) Capital Expenditure (estimated) for approved projects—	
(i) Sites and Buildings (8.2 million sq. ft. estimated factory area)	28.194
(ii) Machinery and Equipment	37.608
(iii) Working Capital	21.162
	86.964
(c) Employment Potential (estimated) for approved projects—	
(i) Male	23.840
(ii) Female	15.860
Total	39.700

6. Apart from non-repayable grants, loan capital for industry can be obtained from the commercial banks in Ireland or from the Industrial Credit Company Limited, a Government-sponsored finance house operated on a commercial basis. This Company makes

capital available to industry by way of medium and longterm loans, direct share investment and hire purchase finance. It also acts as an underwriter for capital issues by public companies.

In the eight-year period ended 31st March 1967 the Industrial Credit Company advanced capital to industry totalling £25m., the vast proportion of which was by way of loan capital.

OTHER INCENTIVES AND FACILITIES FOR INDUSTRIAL DEVELOPMENT

7. Company profits in Ireland are subject to direct taxation amounting to a maximum of 50% (approximately) of net profits. There is complete exemption, however, from taxes on profits derived from goods exported by new industries for a period of ten years (until 1983 in the case of industries located at Shannon Free Airport).

In present circumstances, Ireland's most important asset for industrialists is, perhaps, the availability of workers. Although unemployment and emigration have fallen, there are still considerable labour resources available for industrial employment, a position which is likely to continue for some years to come. Labour costs compare favourably with other West European countries while the cost of fringe benefits and social charges as a percentage of total wage costs is one of the lowest in Europe amounting to about 12.5%.

8. Ireland has an extensive power network extending into every part of the country. There is a well-developed internal transport system, excellent roads and frequent sea and air services between Ireland and the major ports of Europe, U.S.A. and other areas of the world. Excellent industrial sites are available throughout the country offering convenient facilities with regard to transport, water, power and labour supply. The Free Trade Area Agreement with Britain which became effective from 1st July, 1966 ensures duty-free access to the British market for Irish exports—an ideal opportunity, therefore exists for industrialists establishing plants in Ireland to exploit the benefits which are expected to accrue from this agreement.

9. Industrial Estates—The first Government-sponsored industrial estate was established within the Customs-Free Airport at Shannon where special facilities are offered to industrialists. Factories are built in advance of occupation by the Shannon Free Airport Development Company Limited, which is a Government-sponsored body entrusted with the responsibility for the development of Shannon Free Airport. These factories are made available to industrialists at attractive rents but if a manufacturer so wishes he may have his own factory built with the aid of a grant. The aim is to attract industries to Shannon which can benefit from the extensive air service available to many parts of the world though of course it is not essential that their output should be transported by air. The Shannon Industrial Estate has grown rapidly and affords employment to over 3,500. The Government has decided that further industrial estates with factories for renting should be established at selected development centres and that public funds should where necessary be made available for his purpose. In advance of the completion of the regional surveys which are being undertaken by the Minister for Local Government for the purpose of identifying development centres in each region, industrial estates are being set up by An Foras Tionscal at Galway and Waterford. Industrialists will have the option of leasing factories at attractive rents or purchasing them outright with the aid of grants. Grants may also be provided towards the cost of new machinery and the training of

workers. Ready-built factories at attractive rents are also available in many private industrial estates.

In their Economic Survey of Ireland, the O.E.C.D. have made the following comments on the Irish economy:
"The Structure of the economy appears to be basically favourable to growth. Ireland is one of the rare countries in Western Europe to have a surplus of manpower at the present time. Yet in other respects the country is on a par with economies whose degree of development is more advanced, notably as regards educational standards, public and private attitudes to social and enonomic problems, and the existence of an extensive infrastructure. The country is, furthermore, well placed geographically to serve the major European and North American markets. The extent to which Ireland has been able to attract foreign capital and to increase exports of agricultural and, in particular, industrial products in recent years, attests the importance of these factors".

MORE DETAIL. It is felt that in order to present a fairly clear and comprehensive picture an article of this nature should contain a reasonable amount of detail to supplement the general matters already mentioned at least as regards the most important items.

INCENTIVES FOR NEW INDUSTRIES
AN FORAS TIONSCAL—GRANTS FOR INDUSTRIAL DEVELOPMENT

1. AN FORAS TIONSCAL is a corporate body constituted under the Undeveloped Areas Act, 1952. It administers the Undeveloped Areas Acts, and the Industrial Grants Acts.

2. Grants are available from An Foras Tionscal for the establishment or development of industrial undertakings in (a) the Undeveloped Areas and (b) in the remainder of the State, excluding Shannon Free Airport.

3. Grants are available as follows towards (a) the cost of factory sites, site development, factory buildings, and machinery and equipment, (b) the training of workers, and (c) the cost of providing electricity supply:

A TOWARDS THE COST OF A FACTORY SITE, SITE DEVELOPMENT, FACTORY BUILDINGS, AND MACHINERY, PLANT AND EQUIPMENT

(i) In the Undeveloped Areas: A grant of up to two-thirds of the total of such costs.
(ii) In the areas outside the Undeveloped Areas (but excluding Shannon Free Airport): A grant of up to one-half of the total amount of such costs, but where An Foras Tionscal are of the opinion that there are sound economic reasons why the undertaking cannot be established or developed in the Undeveloped Areas and other exceptional circumstances exist a grant of up to two-thirds of the total amount of such costs can be made.

GRANTS IN EXCESS OF £250,000
(a) A grant in excess of £250,000 may not exceed one half of the total amount of such costs, or a sum equivalent to £1,000 multiplied by the number of persons that in the opinion of An Foras Tionscal, will be employed in the undertaking when in full production, whichever is the less.
(b) A grant in excess of £500,000 may not be made without the consent of the Minister for

Industry and Commerce and the Minister for Finance.

(c) The Government may approve the making of a grant which exceeds £250,000 and exceeds the limits set out in the foregoing.

(iii) Guarantee the payment of money payable to the Electricity Supply Board in respect of the capital cost of the provision of electricity supply.

4. Grants may also be made in aid of an industrial undertaking for the construction and repair of roads, bridges, harbour works, railway lines and facilities for the provision of canteens etc.

5. For a project located in the Undeveloped Areas provision is also made to empower Local Authorities to grant two-thirds remission of rates for 10 years on premises provided by means of a grant by An Foras Tionscal.

ADAPTATION GRANTS

In respect of applications made before 30th September 1967 and approved before 31st December 1967, An Foras Tionscal was empowered to give Adaptation Grants towards the enlargement of an industrial undertaking or the adaptation of its machinery, plant, equipment, buildings, or other works, so as to enable the undertaking to be carried on more efficiently or to enable it to engage in the manufacture of products not manufactured by it before the making of the enlargement or adaptation (the grant could not exceed 25% of the cost of the enlargement or adaptation).

The earlier of the two critical dates just quoted has, of course, passed already and it is not yet known if the Government will (as they did last year) extend the scheme for a further period. Accordingly this brief 'Adaptation Grants' section has been included basically for general information. Interested industrial promoters should enquire as to the exact position at the time they are building up a proposal.

It is recognised that large projects may involve heavy capital expenditure and give relatively little employment, and in these cases special arrangements for grants and other financing may be made. Subject to the industrialist providing not less than one-third of the cost of the fixed assets, the balance may be provided by a combination of a grant, a special loan, and a commercial loan from the Industrial Credit Co. Ltd. equal to the amount of the special loan. The special loan would be repayable only at the option of the borrower, would not entail a charge on the assets, would be free of interest for 7 years and thereafter would bear interest at a rate which would increase according as ordinary dividends exceeded 7½%.

Individual grants have varied from a few hundred pounds to as much as £½ million, each project being assessed on the basis of its estimated contribution to the Irish economy. Grants are given by a special Grants Board set up by the Government for the purpose. The members of the Board are appointed by the Minister for Industry and Commerce. The Board is independent and takes its own decisions within the limits laid down by law. In considering an application for a grant, the Grants Board require a full description of each project, with details of the principals, the size and cost of the project, the numbers to be employed, etc. The key questions which they ask may be summarised as follows:-

(a) Have the principals the qualifications and the experience needed in the industry they are proposing to set up?

(b) Have they established by an investigation that the projected industry can be operated economically and profitably in Ireland?

(c) Can they show that markets are available

for the goods to be produced and that they will be able to dispose of their output economically in these markets?
(d) How much money will the principals invest directly in the industry?
(e) Will the new industry injure any existing Irish firm on the Irish market?
An important point to be kept in mind is that, by presenting an application with the necessary details, an industrialist can get a binding decision in principle on the grant application before he commits himself to any expenditure for the purchase of land, formation of company, ordering of machinery etc. The decision on a grant is normally given by way of a letter and is implemented in accordance with a contract between the Grants Board and the company. In the contract, one important condition is that the recipient agrees not to sell the business for 10 years without the consent of the Grants Board. There are no other strings attached—there is no question of Government supervision or representation on the Board.

B TOWARDS THE COST OF TRAINING WORKERS

Grants are available towards the cost of training, either in the State or elsewhere of workers in skilled processes of an undertaking. The amount of such grant may not exceed the actual amount of the wages paid by the undertaking to the trainee workers during their period of training together with, in the case of workers trained outside the State, the amount of their expenses of travel and subsistence.

C TOWARDS THE CAPITAL COST OF THE PROVISION OF ELECTRICITY BY THE ELECTRICITY SUPPLY BOARD (E.S.B.)

Where a grant is made towards the cost of providing buildings, or machinery and equipment, An Foras Tionscal may make a grant towards the capital cost of the provision of electricity by the E.S.B. Any such grant made may not exceed one-half of the capital cost payable to the E.S.B.

GUIDE TO THE SUBMISSION OF INDUSTRIAL PROPOSALS

1. PRINCIPALS
The name and address of the firm; brief note on history of the firm; products manufactured; value of annual output, exports and employment.

2. PRODUCTS
What articles will be manufactured in Ireland and what are the manufacturing processes?

3. PRODUCTION
What is (a) the expected annual output at full production in quantity and value and (b) the expected level of output at the end of the first year of production. From the commencement of manufacture how long will it take to reach full production?

4. LOCATION
Where will the factory be located?

5. SITES AND BUILDINGS
(a) If it is intended to build a factory state extent and expected cost of site. What is the floor area of the building required? Give a short description—number of floors, type of construction etc. Are they any special features in the building? What is the estimated cost of buildings and site development (see also 15 c below).

(b) If it is intended to rent or purchase a factory give particulars of (i) floor area (ii) rent and period of lease, or purchase price.

6. MACHINERY AND EQUIPMENT

Specify the major items of machinery and equipment indicating the estimated cost in each case.

Note: Plant and machinery should be new. Cost of office equipment and external transport should be shown separately as these are not eligible for grants.

7. RAW MATERIALS AND PARTS

What percentage of the value of output will be represented by (a) raw materials and parts and (b) imported raw materials and parts? For the principal raw materials and parts state the quantities which will be needed at full production (3 a above), the cost and where they will be obtained.

8. EMPLOYMENT

What is the expected employment at (i) full production (3 a above) and (ii) at the end of the first year of production (3 b above)? Give separate figures for male and female workers and the number and type of skilled workers for (i) and (ii). If it is intended to bring in technicians please state how many.

9. MANAGEMENT AND TECHNICAL CONTROL

What are the plans for management of the company and for technical control of pro-production?

10. FINANCE

A. Give estimated requirements for:-

(i) fixed assets (under the following heads):-

Site	see par. 5
Site Development	see par. 5
Building	see par. 5
Machinery and equipment	see par. 6

Total for fixed assets.

(ii) office equipment and external transport, if any

(iii) working capital.

B. How is it proposed to provide the capital required for:-

(i) fixed assets (under the following heads)-
Amount to be provided by the principals
Amount sought by way of grant
Amount to be provided by borrowing (if any) and from whom;

(ii) office equipment and external transport;

(iii) working capital.

11. EXPORT MARKETS

(a) What proportion of the annual output of the proposed factory will be exported and to what countries?

(b) Give particulars of exports by the principals to each of the countries at (a) in each of the last three years.

(c) It is important that any additional information showing the market prospects should be given.

12. IRISH MARKET

Information regarding sales on the Irish market (if any) should be given.

13. ROYALTIES OR OTHER PAYMENTS

Will any royalties, commissions or fees be payable to external interests in connection with the project?

14. EFFLUENT

Will there be any noxious effluent? If so, what arrangements will be made for its disposal and has the cost been included in the estimate of building costs at 5 above.

15. Before a grant can be approved the following will also be required:-

(a) Certified Balance Sheets and Profit and

Loss Accounts for the latest available three years.

(b) An assessment of the profitability of the project in the form either of (i) an estimated costing of a representative product to be produced compared with the cost of producing it in the parent factory of (ii) a projected profit and loss account covering the operation of the proposed factory in the first year of full production.

(c) If it is intended to build a factory a statement from an Irish architect that he is satisfied in relation to the estimate of the cost of buildings. Items which may have to be considered in making preliminary estimates of building costs are set out in the following statement.

BUILDING COSTS

1. SITE

Having determined what acreage of land would be required for immediate factory requirements, with provision for expansion for a reasonable period ahead, the promoter should make discreet enquiries as to the sale value of land in the area he has in mind. Site costs vary very considerably from one place to another depending on whether the site would be in an urban or rural area and the demand for land in the district.

2. SITE DEVELOPMENT

Under this head provision should be made for the cost of any of the following which may be needed:-

(i) Land levelling
(ii) Drainage
(iii) Sewerage from the factory site to the nearest public sewerage system.

If the latter is not near the site, enquiries should be made as to whether the local authority concerned would be prepared to bring the public system to the nearest road-point to the site and if so whether this would be done free of cost.

(iv) Factory effluent as distinct from normal sewerage for sanitary purposes. If there should be a factory effluent discharge the question arises as to means of disposal. Will the Local Authority permit discharge through the public sewerage system; if so, agreement in writing should be obtained. If the public disposal system cannot be used consideration has to be given to what alternative means can be adopted and the estimated cost. In considering effluent discharge into rivers or river mouths or estuaries consideration has to be given as to whether there is any danger to animal or fish life.

(v) Roads:- e.g. approach roads through the site to the factory and where necessary other roads within the site.

3. BUILDING SERVICES

(i) Water Services:-

(a) The availability of adequate and suitable water supplies should be investigated, and the cost estimated.

(b) The availability of sufficient water pressure to deal with an outbreak of fire should be investigated. In this connection the requirements of Insurance Companies for the purpose of insurance against fire should be ascertained and taken into account.

(ii) Electricity Supply: Where appropriate the availability of electricity supply of the necessary strength for power should be investigated and enquiries should be made as to any Capital Charges which the E.S.B. might make for the provision at the site of the necessary supply. The cost of providing at the site electricity supply for lighting and heating, in so far as this may be a separate item should be ascertained.

(iii) Transformers: If the provision of a transformer should be necessary the cost should be estimated.

(iv) Telephone Services: If there should be a charge for bringing the service to the site the estimated cost should be ascertained.

(v) Special Roads, tracks, etc.: Where necessary, provision for special roads within the site, concreted areas for outdoor storage, sunken rail tracks for trucks or gantry, etc.

4. FACTORY BUILDING (i.e. production areas).

i.e. (i) working space
(ii) offices
(iii) toilets and canteen if the latter should be necessary and bearing in mind that elaborate canteens are not needed in Ireland
(iv) Store rooms
(v) Boiler House (if necessary)
(vi) Showroom (if necessary)
(vii) Garages and bicycle sheds
(viii) Any special finishes which may be necessary for special purposes connected with the processes e.g. tiling, special floors or special hard floor surfacing.
(ix) In planning the factory it is advisable to make it as fire resistant as possible and thus obviate high insurance rates.

5. MECHANICAL SERVICES

(i) Electrical wiring system for lighting and lighting fittings.
(ii) Any special wiring for power to a main switchboard (Note:- the wiring up of machines from a main switchboard is regarded as part of the machinery and equipment and not as a building service.)
(iii) Heating distribution system e.g. hot water piping, and radiators etc. to factory working space and offices.
(iv) Boiler for heating.
(v) Ducting, for dust extraction, where necessary.
(vi) Air-conditioning, where necessary for particular processes.
(vii) Any other special building fixtures which may be necessary for the special requirements for the industry e.g. special air vents, air or dust extraction, fans which are built in as fixtures in the building, overhead gantry rails, floor truck or gantry rails etc., all of which are readily detachable without interfering with the building structure would be regarded as equipment. All motors and mechanisms which are connected with such special provisions and which are removable are regarded as equipment and not building services.
(viii) A boiler for steam for processing is regarded as plant.

6. GENERAL

(i) Septic tanks, where needed.
(ii) Water and/or storage tanks, in concrete or steel, fixtures.
(iii) Settling tanks for effluent (exclusive of pumping installations which would be part of plant and equipment).
(iv) Architects' fees for plans and specifications of buildings and supervision of building works.
(v) Quantity Surveyor's fees for drawing up Bill of Quantities.
(vi) Engineer's fees where necessary in connection with mechanical services for the buildings.
(vii) Legal fees in connection with the acquisition of the site.

Importation of Machinery and Raw Materials

New firms are allowed to import their machinery free of duty. Raw materials for export trade are also allowed in duty-free whether they can be got in Ireland or not.

Transfer of Profits, Dividends and Capital

Investors are guaranteed freedom to transfer their profits and dividends at any time and to repatriate their capital whenever they wish.

Man-Power

The natural increase in the Irish population (the excess of births over deaths) is about 30,000 per annum. The number of unemployed approximately 47,000 is not excessively high. In Ireland, as in other countries, the numbers employed in agriculture have steadily fallen throughout the years, as farmers have turned more and more to the use of mechanical methods. There is accordingly in Ireland a substantial surplus of tranaible labour in almost all parts of the country.

There is also a large pool of Irish workers in Great Britain who have acquired considerable experience in different industrial fields. Many of these are anxious to return home if employment can be found.

There is also a supply of University graduates, including engineers, chemists, economists, doctors, etc. About 2,000 students graduate annually from the Irish Universities, and in the past a large proportion of these have been forced to seek employment abroad because of lack of opportunities at home.

EMPLOYMENT OF WORKERS FROM ABROAD

Work permits are needed for workers from outside Ireland. Permits are readily granted for technicians from abroad for as long as they may be needed.

LABOUR RELATIONS

Wages and conditions of work are normally regulated by collective bargaining between employers, or their organisations, and trade unions. There is no minimum rate of wages laid down by the State. Wages generally are much lower than in the United States, and lower also than those prevailing elsewhere in Western Europe. For example, in Ireland an electrician earns 76 pence an hour, a motor mechanic (repair man) earns up to 76 pence an hour, whilst a woman employed on factory work will normally earn about 36 pence an hour.

A Labour Court, established by the State, on which both employers and trade unions are represented under a neutral Chairman, assists in keeping industrial peace. The Court's recommendations have not the force of law and may be accepted or rejected by either party to the dispute before it. In addition, the Court operates a conciliation service, to help the opposing parties in disputes to reach agreement. Employers are free in law to "hire and fire" in accordance with the needs of their firm; a man need not be retained if there is no work for him. The law requires that every worker shall be given twelve working days holidays per year in respect of a full year's employment (and fringe-benefit deals are at present being negotiated to increase this). In addition there are six public holidays during the year. The State operates a compulsory social welfare insurance scheme for all manual workers and for all non-manual workers whose income does not exceed a stated sum. The scheme is financed by weekly contributions by employers and employees and by an annual subvention by the State.

SERVICES IN IRELAND

A State-owned body, the Electricity Supply Board, provides a nation-wide service of electric power. Power is available in all parts of the country from a national grid and at prices uniform throughout the country.

Prices of power are broadly comparable with those in Europe as a whole. Rail and road transport services are provided by a national transport company, but independent road hauliers also operate. Companies may, of course, use their own transport for the carriage of their own goods. Roads in Ireland are good and there is a very extensive network. Shipping services operate between the principal ports and U.S.A. and Canada, Britain, Europe, North Africa, the Middle East and the West Indies. Water supplies and sewerage facilities are available in all towns and cities.

PROCEDURE FOR COMPANIES INTERESTED IN THE REPUBLIC OF IRELAND

There is no hard and fast routine to be followed, but experience shows that the natural sequence of events is as follows:-

(a) The interested company makes contact with the Irish Industrial Development Authority. Preliminary information on Ireland and on the opportunities for the company's particular industry is obtained quickly through discussion or correspondence.

(b) Representatives of the firm visit Ireland for more detailed discussion with the Industrial Development Authority and also for an examination in depth of the country and the collection of detailed information on wages, etc. pertaining to the particular industry.

(c) A survey is carried out to confirm that manufacture in Ireland is economic and profitable, and a location for the proposed factory is selected.

(d) A proposal outlining the project for Ireland is prepared and put before the Industrial Development Authority. If no financial assistance is sought from the Irish Government and if the project is for export, the company is at this stage normally free to go ahead as soon as it wishes. If the company seeks financial assistance by way of a non-repayable grant, the Authority puts the proposal before the special Grants Board for a decision.

(e) The Grants Board will normally interview the applicant and convey its decision on the spot. This decision is then confirmed in writing and a draft contract is forewarded shortly afterwards. The company is then in a position to arrange for the acquisition of a site, the formation of an Irish company (if they so desire) and the construction of a factory.

TAXES AND TAX RELIEF

INCOME TAX

The Income Tax system and the principles of taxation in force in Ireland are basically similar to those in the United Kingdom prior to the U.K. Finance Act 1965. Except for a few modifications the Income Tax law was the same in both countries up to and including the Finance Act of 1922. That law and Irish Finance Acts, 1923 to 1967, constitute the present Income Tax law of Ireland.

Income tax is payable by individuals and companies on income or profits.

Standard rate: 7s.0d. in the pound (35%)

Individual taxpayers receive deductions from income:-

Earned Income Allowance: maximum allowance £500 personal and childrens allowance.

CORPORATION PROFITS TAX

Companies liable are those incorporated under the law of the Irish Republic and carrying on a trade or business. Foreign companies established in the Republic are also liable in respect of profits which arise in the Republic.

Rates of tax: 7½% on the first £2,500 of profits;
23% on the balance of profits in excess of £2,500.

The Corporation Profits Tax payable is allowed as a deduction when computing profits liable to Income Tax. The combined effect of Income Tax and Corporation Profits Tax is therefore a tax rate which varies from 40% (approximately) for very small profits to 50% (approximately) for large profits.

SURTAX

This is an additional tax on the incomes of individuals. It is chargeable on incomes which, after making certain deductions, are in excess of £2,500.

	Rates of Surtax in the £.
In respect of the first £2,000 of the chargeable income	2s.6d.
In respect of the next £3,000 of the chargeable income	5s.0d.
In respect of the balance of the chargeable income	7s.6d.

DEFINITION OF INCOME OR PROFITS

There is no general definition of income. Capital profits or gains are not taxable. Notional valuations of income are adopted in the case of income from the ownership of land and buildings. These are based on the "annual value" i.e. an assessed theoretical rental value, and are low in relation to current rental values. There are allowances for repairs.

Profits from a trade or business are generally determined by applying the ordinary principles of commercial accounting, subject to the statutory rule that any expenditure deductible from profits for tax purposes must be expenditure "wholly and exclusively laid out for the purposes of the trade", that is, for the purpose of earning the profits.

Dividends are paid out of taxed profits.

RELIEF FROM TAX IN RESPECT OF PROFITS FROM EXPORTS

Profits attributable to increased export trade in Irish manufactured goods are eligible for complete relief from Income Tax and Corporation Profits Tax for ten consecutive years. In the case of a new company manufacturing in Ireland for the first time exports would represent a 100% increase so that the tax relief would be applied to the whole of the profits attributable to export sales. The year of assessment 1979/1980 will be the last year for which the 100% relief will be granted. A company whose first year of claim occurs in any year up to and including 1970/1971 would, therefore, be entitled to a full ten years period. A company commencing an export trade after 1970/1971, would obtain full relief for the remaining years up to 1979/1980.

Companies commencing an export trade before 1970/1971 would in addition to ten years' full relief, be entitled to a further period of partial relief.

A company, which has obtained export profits tax relief, passes on a similar measure of relief from Income Tax and Sur-tax to shareholders when it distributes a dividend. For the purposes of the relief, the profits attributable in any year to export trade are calculated by apportioning the companies total profits for the year from goods sold in the same ratio as the total sales (value) of the goods exported bears to the sales (value) of all the goods sold whether exported or not.

Special tax relief is afforded in the case of industries set up in the Shannon Free Airport Zone. This relief gives freedom from tax on the profits of exempted trading operations up to 1983.

DEPRECIATION

In calculating profits for Income Tax and Corporation Profits Tax purposes deduc-

tions are permitted in respect of the depreciation of fixed assets, used during the year for the purpose of the trade, as follows:

PLANT AND MACHINERY

(a) Initial Allowances may be deducted in respect of capital expenditure during the year on the provision of new machinery or plant (excluding road vehicles) or of ships whether new or second-hand, for the purposes of the trade. The amount of the allowance is 40% of the expenditure. (Note: In the case of new ships there is the alternative of a 40% "investment allowance".)

(b) Annual Allowances may be claimed in respect of wear and tear of machinery and plant. The basic allowances vary in accordance with the estimated useful life of the different types of machinery or plant. They are calculated to write off the cost of the asset over its life. As an aid to industrial development the basic rates have been increased by one fourth (except in the case of road vehicles).

INDUSTRIAL BUILDINGS

(a) An Industrial Buildings Allowance may be claimed in respect of capital expenditure incurred by a trader on or after 30th September 1965, on the construction of an industrial building or structure. The amount deductible from profits is 20% of the expenditure. For this purpose docks, wharves, piers, jetties, etc., rank as industrial buildings or structures and expenditure on cutting and levelling of land in the course of preparing it as a site for a factory is regarded as part of the cost of constructing the factory.

(b) An Annual Allowance of 2% of the expenditure may be deducted in the case of industrial buildings which qualify for the Industrial Buildings Allowance described above because of expenditure incurred on or after 30th September 1965.

(c) Balancing allowances and charges. On sale of an industrial building in respect of which Industrial Buildings Allowance and Annual Allowances have been given as described above, any deficiency or excess in the allowances as compared with the price realised is adjusted by means of balancing allowances or balancing charges.

Patent Rights

Capital expenditure incurred on the purchase of patent rights or on the acquisition of a licence or patent rights may be claimed in computing profits for tax purposes.

Capital Expenditure on Scientific Research

Expenditure may be claimed against the profits of the year in which the expenditure is incurred.

DOUBLE TAXATION

Double Taxation treaties exist with Great Britain, Germany, U.S.A., Canada, Denmark and Sweden, and negotiations are in progress to extend the number of treaties.

IMPORTANT NOTE: For obvious reasons, not the least of which is the time element involved, interested parties must check up on all taxation and other aspects at the time of contract,

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The industrial potential of Ireland Ireland as a location for industry Ireland your manufacturing base in Europe Industrial Incentives in Ireland ("Keynote talk by a Director") Taxes and Tax reliefs in Ireland Export profits tax relief Factories for renting at Galway and Waterford Guide to the submission of industrial proposals (quoted in article)	The Industrial Development Authority
Shannon as a project location	Shannon Free Airport Development Co. Ltd.
Guide to State aids and services for Irish industry	Department of Industry & Commerce (Industrial Reorganisation Branch)

Note: The well-known American agency "Business International" which advises international business on foreign investment recently published a check list of 92 factors for consideration by any company contemplating the establishment of manufacturing operations abroad. Their special booklet "Manufacturing in Ireland" lists the relative factors and gives factual comments on them in relation to the Republic of Ireland. (The 24 page booklet had considerable interest in the context of this article but was considered too long for quotation in extenso. It is available from the Industrial Development Authority.)

NORTHERN IRELAND

Under it's Industries Development Acts, the Northern Ireland Ministery of Commerce "intends to ensure that the terms offered for the expansion of employment in Northern Ireland continue to be the most attractive in the United Kingdom". The implementation of this laudable intention is to be mainly through outside investors of whom a number—some sizable—have already been attracted in. While there has been an encouraging "capital grants to industry" scheme in operation for some years past, there will, by the time that this paper is being considered, be an improved scheme providing (in addition to all normal encouragements) special Investment Grants towards the cost of sites, buildings and new plant and machinery—up to 40%. In addition there will be financial facilities in connection with operating costs (an especially valuable concession), training costs etc. As an alternative to building specially there are available 'ready-to-occupy' factories at very low rates and rent.

Broadly speaking and necessarily oversimplifying to some extent, the determination of the Northern Ireland Government and the type of facilities being made available for the establishment of industries are parallel

to that obtaining in the Republic of Ireland. The relative authority is MINISTRY OF COMMERCE, 64 CHICHESTER STREET, BELFAST 1, NORTHERN IRELAND.

Full documentation is freely available from the Ministry Officials—it includes the following:

1. "GOVERNMENT SPONSORED INDUSTRY"
2. "REPORT ON INDUSTRIAL DEVELOPMENT FACILITIES IN NORTHERN IRELAND"
3. "CAPITAL GRANTS TO INDUSTRY"
4. "INDUSTRIAL ADVICE GRANTS SCHEME"
5. "A SERVICE TO INDUSTRY (TRAINING ON EMPLOYERS' PREMISES)"
6. "GOVERNMENT SPONSORED INDUSTRY".

CONCLUSION

I wish to express the hope that this modest contribution from Ireland may be of help in completing the desired overall picture and of interest to professional accountants abroad. While it was necessary to give a reasonable amount of detail in some sections it was conversely not possible to elaborate the more general concepts dealt with earlier on. Indeed the full development of quite a number of the important aspects dealt with, of necessity rather briefly, would have provided the material for many full-scale papers.

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In the series "Trattato di Scienza delle finanze" volume IX SISTEMI FINANZIARI COMPARATI, by Gangemi, L. has been published by UTET, Turin, 1967.
Our correspondent G. Croxatto writes the following about this book:
This important and extensive work contains a thorough exposition and comparison of the financial systems of the most significant states of the world. The entire work will comprise three volumes of which the first two have now been published. The author divides the states examined in three categories according to their political, social and economic conditions. The first group includes the industrialized countries, including the member states of the EEC, to which the entire first volume is devoted. This volume is of particular interest in the view of the harmonization and comparison of the fiscal system of the Six. Classified among the industrialized states are Great Britain, United States, Sweden, Switzerland and Japan and their financial systems have been described in detail.
Described in the second group are those countries with collective economic systems: the Soviet Union and Yugoslavia, which are particularly representative of this type of state since, notwithstanding their similar economic system, they differ considerably with respect to State organization and in degree of economic and industrial development. Finally the third group includes the underdeveloped countries, to which the third volume—to be published shortly—will be entirely dedicated. The exposition of the financial systems of each country is introduced by an indication of the political and economic aspects of the states examined, and a short description of the evolution of its financial system. An analysis is then given of the organization of the public administration in the financial sector, of the Budget and of public enterprises. The largest part is of course reserved to a description of the individual tax systems, which is completed by useful statistical data and by a rich bibliography. It should further be noted that the work contains an interesting introduction indicating the common trends in the evolution of the financial systems subjected to discussion, apparent from the pre-country analysis.

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Projet de Convention tendant à éliminer les doubles impositions et à établir les règles d'assistance mutuelle administrative en matière fiscale entre les Etats francophones d'Afrique Noire

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INTERNATIONAL BUREAU OF FISCAL DOCUMENTATION

Muiderpoort – 124 Sarphatistraat – Amsterdam

INTRODUCTION

La France a, durant ces dernières années, conclu des conventions fiscales avec un grand nombre de pays africains. Il s'agit notamment des conventions conclues avec Madagascar (du 29 septembre 1962), la Côte d'Ivoire (du 5 avril 1965), le Gabon (du 21 avril 1965), le Sénégal (du 3 mai 1965), le Niger (du 1 juin 1965), le Cameroun (du 10 juillet 1965), la Haute Volta (du 11 août 1965) et le Dahomey (du 21 octobre 1965). Des négociations sont en cours avec le Congo Brazzaville, la Mauritanie, la République Centrafricaine, le Tchad, le Togo, l'Algérie et le Maroc.

Toutes ces conventions portent sur les impôts sur le revenu, les impôts sur les successions, ainsi que sur les droits d'enregistrement et de timbre. En principe, les conventions sont identiques. Le texte des plus anciennes conventions est sur quelques points moins détaillé que celui des plus récentes. Des exemples peuvent en être pris, d'une part, dans la convention avec Madagascar, conclue en 1962 et entrée en vigueur le 1er juin 1965, après un échange de lettres du 14 mai 1965[1]) et, d'autre part, la convention plus récente avec le Cameroun[2]). Les conventions ont subi la très forte influence du projet du convention fiscale multilatérale entre les Etats francophones de l'Afrique Noire, projet qui fut le résultat d'une conférence tenue à Abidjan (Côte d'Ivoire) en juin 1963 dans le cadre de l'Organisation Africaine et Malgache de Coopération Economique (O.A.M.C.E.).

Le texte de ce projet paraît dans le présent Supplément. Nous pensons que ce texte est une indication quant au contenu des conventions bilatérales que la France a conclues, ou

1) Voir ce Bulletin, Vol. XIX (1965), p. 459 et suiv.
2) Voir ce Bulletin, Vol. XX (1966), p. 470 et suiv.

se propose de conclure dans un proche avenir, avec les pays africains. Le projet de l'O.A.M.C.E. a fait l'objet d'une recommandation de la 5ème conférence des Chefs d'Etat de l'Union Africaine et Malgache qui s'est tenue à Dakar du 3 au 10 mars 1964. Cette recommandation est restée sans effet pratique, raison pour laquelle le texte n'en est pas reproduit ici.

Un bref aperçu de la conférence de Dakar fut publié par la revue «Information d'Outre-Mer» du 1er juillet 1964 communiqée par le Centre d'Etudes d'Outre-Mer[3]) sous le titre «Convention interafricaine relative à l'élimination de doubles impositions».

Il est intéressant de noter que le pendant du projet de convention fiscale multilatérale entre les pays francophones de l'Afrique Noire est celui intitulé «Commonwealth Taxation Agreement» (Modèle de Convention Fiscale du Commonwealth Brittanique)[4]).

La problématique fiscale prend de plus en plus forme en Afrique, tel qu'il en ressort du «Cycle d'Etudes de Niveau Supérieur sur les Problèmes Actuels et les Besoins de Formation dans le Domaine de l'Administration Fiscale», organisé par la Commission Economique pour l'Afrique des Nations Unies à Addis-Abéba du 6 au 15 décembre 1965. Le fait que beaucoup de pays africains, francophones et anglophones, y étaient représentés est réjouissant. L'objectif de ce Cycle était de permettre un échange de vues entre les chefs des services fiscaux sur les principaux problèmes qui se posent actuellement à eux et sur les moyens de renforcer les administrations fiscales africaines en fonction des tendances actuelles. Les organisateurs du Cycle avaient suggéré d'accorder une attention particulière aux questions relatives au recrutement et aux problèmes de formation du personnel employé dans les administrations fiscales, à la nécessité de réformer les systèmes fiscaux et aux domaines dans lesquels une aide extérieure est immédiatement nécessaire aux administrations[5]).

Un des problèmes de grande actualité pour les gouvernements africains est d'adapter leurs lois fiscales aux besoins d'une économie moderne tout en tenant compte de la situation socio-économique qui existe, dans différents degrés, dans leurs pays respectifs. Une des recommandations du Cycle était de faire une étude approfondie des aspects internationaux généraux de la fiscalité, y compris les rapports avec les pays dévéloppés exportateurs de capitaux; de faire des études comparatives et analytiques des régimes fiscaux en Afrique; de faire le ons nécessaire pour arriver à une collaboration et une harmonisation des administrations fiscales en Afrique.

Il est à souhaiter que ce Cycle d'Etudes contribue dans les Etats africains à une réforme harmonieuse de leurs systèmes fiscaux sur la base d'une entente mutuelle, compte tenu des relations avec les pays industrialisés. Ceci pourrait leur donner l'avantage de former un groupe uni lors de délibérations avec d'autres pays pour arriver à la conclusion de conventions fiscales bilatérales. Déjà existe-t-il une large mesure d'uniformité dans la législation francophone. L'harmonisation n'en est pas handicapée par un long passé de développement traditionnel pour chaque pays, comme cela est le cas en Europe. Ce qui est largement démontré par le projet que nous avons le plaisir de reproduire dans ce Supplément.

3) Adresse: 12, Rue Margueritte, Paris (17e).
4) Voir ce Bulletin, Vol. XVIII (1964), p. 409 et suiv.
5) Déclaration du Secrétaire exécutif de la C.E.A. dans la lettre de convocation du 3 août 1965.

Texte

du Projet de Convention tendant à éliminer les doubles impositions et à établir les règles d'assistance mutuelle administrative en matière fiscale entre les Etats francophones d'Afrique Noire

---

Les Etats signataires de la présente convention,

Désireux d'éliminer les doubles impositions et d'établir des règles d'assistance mutuelle administrative en matière fiscale,

Sont convenus des dispositions suivantes:

TITRE PREMIER

DISPOSITIONS GENERALES

Article 1er

Pour l'application de la présente convention, le terme «personne» désigne:

a) toute personne physique;
b) toute personne morale;
c) tout groupement de personnes physiques qui n'a pas la personnalité morale.

Article 2

1. Une personne physique est domiciliée, au sens de la présente convention, au lieu où elle a son «foyer permanent d'habitation», cette expression désignant le centre des intérêts vitaux, c'est-à-dire le lieu avec lequel les relations personnelles sont les plus étroites.

Lorsqu'il n'est pas possible de déterminer le domicile d'après l'alinéa qui précède, la personne physique est réputée posséder son domicile dans celui des Etats contractants où elle séjourne le plus longtemps. En cas de séjour d'égale durée dans plusieurs Etats elle est réputée avoir son domicile dans celui des Etats dont elle est ressortissante. Si elle n'est ressortissante d'aucun d'eux, les autorités compétentes des Etats trancheront la difficulté d'un commun accord.

2. Pour l'application de la présente convention, le domicile des personnes morales est au lieu du siège social statutaire; celui des groupements de personnes physiques n'ayant pas la personnalité morale au lieu du siège de leur direction effective.

Article 3

Le terme "établissement stable" désigne une installation fixe d'affaires où une entreprise exerce tout ou partie de son activité.

a) constituent notamment des établissements stables:

(aa) un siège de direction;
(bb) une succursale;
(cc) un bureau;
(dd) une usine;
(ee) un atelier;
(ff) une mine, carrière ou autre lieu d'extraction de ressources naturelles;
(gg) un chantier de construction ou de montage;
(hh) une installation utilisée aux fins de stockage, d'exposition et de livraison de marchandises appartenant à l'entreprise

(ii) un dépôt de marchandises appartenant à l'entreprise entreprosées aux fins de stockage, d'exposition et de livraison;

(jj) une installation fixe d'affaires utilisées aux fins d'acheter des marchandises ou de réunir des informations pour l'entreprise.

b) On ne considère pas qu'il y a établissement stable si:

(aa) des marchandises appartenant à l'entreprise sont entreposées aux seules fins de transformation par une autre entreprise;

(bb) une installation fixe d'affaires est utilisée aux seules fins de publicité, de fourniture d'information, de recherche scientifique ou d'activités analogues qui ont pour l'entreprise un caractère préparatoire ou auxiliaire.

c) Une personne agissant dans un Etat contractant pour le compte d'une entreprise d'un autre Etat contractant est considérée comme «établissement stable» dans le premier Etat si elle dispose dans cet Etat de pouvoirs qu'elle y exerce habituellement lui permettant de conclure des contrats au nom de l'entreprise.

d) Une entreprise d'assurance de l'un des Etats contractants est considérée ayant un établissement stable dans un autre Etat contractant dès l'instant qu'elle perçoit des primes sur le territoire dudit Etat ou assure des risques situés sur ce territoire.

e) On ne considère pas qu'une entreprise d'un Etat contractant a un établissement stable dans un autre Etat contractant du seul fait qu'elle y effectue des opérations commerciales par l'entremise d'un courier, d'un commissionnaire général ou de tout autre intermédiaire jouissant d'un statut indépendant, à condition que ces personnes agissent dans le cadre ordinaire de leur activité.

Toutefois, si l'intermédiaire dont le concours est utilisé dispose d'un stock de marchandises en consignation à partir duquel sont effectuées des ventes et des livraisons, il est admis que ce stock est caractéristique de l'existence d'un établissement stable de l'entreprise.

f) Le fait qu'une société domiciliée dans un Etat contractant contrôle ou est contrôlée par une société qui est domiciliée dans un autre Etat contractant ou qui y effectue des opérations commerciales (que ce soit par l'intérmédiaire d'un établissement stable ou non) ne suffit pas, en lui-même, à faire de l'une quelconque de ces deux sociétés un établissement stable de l'autre.

Article 4

Sont considérés comme biens immobiliers, pour l'application de la présente convention, les droits auxquels s'appliquent les dispositions du droit privé concernant la propriété foncière, ainsi que les droits d'usufruit sur les biens immobiliers, à l'exception des créances de toute nature garanties par gage immobilier.

La question de savoir si un bien ou un droit a le caractère immobilier ou peut être considéré comme l'accessoire d'un immeuble sera résolue d'après la législation de l'Etat sur le territoire duquel est situé le bien considéré ou le bien sur lequel porte le droit envisagé.

Article 5

Les ressortissants, les sociétés et autres groupements d'un Etat contractant ne seront pas soumis dans les autres Etats à

des impôts autres ou plus élevés que ceux frappant les ressortissants, les sociétés et autres groupements de ces derniers Etats se trouvant placés dans la même situation.

En particulier les ressortissants d'un Etat contractant qui sont imposables sur le territoire d'autres Etats contractants bénéficient, dans les mêmes conditions que les ressortissants de ces derniers Etats des exemptions, abattements à la base, déductions et réductions d'impôts ou taxes quelconques accordés pour charges de famille.

Article 6

Pour l'application des dispositions contenues dans la présente convention et sauf disposition contraire consignée au protocole qui se trouve annexé, l'expression «autorités compétentes» désigne dans chaque Etat, Le Ministre des Finances de cet Etat ou son Représentant dûment autorisé.

Article 7

Pour l'application de la présente convention par l'un des Etats contractants, tout terme non défini dans cette convention recevra, à moins que le contexte ne l'exige autrement, la signification que lui donnent les lois en vigueur dans l'Etat considéré, en ce qui concerne les impôts visés dans cette convention.

TITRE II

DOUBLES IMPOSITIONS

CHAPITRE IER

Impôts sur les revenus

Article 8

1. Le présent chapitre est applicable aux impôts sur le revenu perçus pour le compte de chacun des Etats contractants, de ses subdivisions politiques et de ses collectivités locales, quelque soit le système de perception.

Sont considérés comme impôts sur les revenus les impôts perçus sur le revenu total ou sur des éléments du revenu y compris les plus-values.

2. Les dispositions du présent chapitre ont pour objet d'éviter les doubles impositions qui pourraient résulter, pour les personnes, (entendues au sens de l'article 1er) dont le domicile fiscal, déterminé conformément à l'article 2, est situé dans l'un des Etats contractants, de la perception simultanée ou successive dans cet Etat et dans d'autres Etats contractants des impôts visés au paragraphe 1 ci-dessus.

3. Les impôts actuels auxquels s'applique le présent chapitre dans chacun des Etats contractants sont énumérés au protocole annexé à la présente convention.

4. La convention s'appliquera aussi aux impôts futurs de nature identique ou analogue qui s'ajouteraient aux impôts actuels ou qui les remplaceraient. Les autorités compétentes des Etats contractants se communiqueront, dès leur promulgation, les modifications apportées à leur législation fiscale.

Article 9

Les revenus des biens immobiliers, y compris les bénéfices des exploitations agricoles et forestières, sont imposables dans l'Etat où ces biens sont situés.

Article 10

1. Les revenus des entreprises industrielles, minières, commerciales, ou financières sont imposables dans l'Etat sur le territoire duquel se trouve un établissement stable.

2. Lorsqu'une entreprise possède des établissements stables dans plusieurs Etats contractants, chacun d'eux ne peut imposer que le revenu provenant de l'activité des établissements stables situés sur son territoire.

3. Le bénéfice imposable ne peut excéder le montant des bénéfices industriels, miniers, commerciaux, ou financiers réalisés par l'établissement stable, y compris, s'il y a lieu, les bénéfices ou avantages retirés indirectement de cet établissement ou qui auraient été attribués ou accordés à des tiers soit par voie de majoration ou de diminution des prix d'achat ou de vente, soit par tout autre moyen. Une quote-part des frais généraux du siège de l'entreprise est imputée aux résultats des différents établissements stables au prorata du chiffre d'affaires réalisé dans chaque Etat.

4. Les contribuables dont l'activité s'étend sur le territoire de deux ou plusieurs Etats peuvent, s'ils ne tiennent pas une comptabilité régulière faisant ressortir distinctement et exactement les bénéfices afférents aux établissements stables situés dans les divers territoires, déterminer le bénéfice imposable dans chacun de ces Etats en répartissant les résultats globaux au prorata du chiffre d'affaires réalisé dans chaque Etat.

Article 11

1. Lorsqu'une entreprise de l'un des Etats contractants du fait de sa participation à la gestion ou au capital d'une entreprise d'un autre Etat contractant fait ou impose à cette dernière, dans leurs relations commerciales ou financières, des conditions différentes de celles qui seraient faites à une tierce entreprise, tous bénéfices qui auraient dû normalement apparaître dans les comptes de l'une des entreprises, mais qui ont été de la sorte transferés à l'autre entreprise, peuvent être incorporés aux bénéfices imposables de la première entreprise.

2. Une entreprise est considérée comme participant à la gestion ou au capital d'une autre entreprise notamment lorsque les mêmes personnes participent directement ou indirectement à la gestion ou au capital de chacune de ces deux entreprises.

Article 12

Les revenus provenant de l'exploitation des entreprises de navigation maritime ou aérienne sont imposés dans les conditions fixées à l'article 10.

Article 13

Sous réserve des dispositions des articles 15 à 17, les revenus des valeurs mobilières et les revenus assimilés (produits d'actions, de parts de fondateur, de parts d'intérêt et de commandites, intérêts d'obligations ou de tous autres titres d'emprunts négociables) payés par des sociétés ou des collectivités publiques ou privées ayant leur domicile fiscal sur le territoire de l'un des Etats contractants sont imposables dans cet Etat.

Article 14

Une société d'un Etat contractant ne peut être assujettie sur le territoire d'un autre Etat contractant au payement d'un impôt sur les distributions des revenus de valeurs mobilières et de revenus assimilés qu'elle effectue du seul fait de sa participation dans la gestion ou dans le capital de sociétés domiciliées dans cet autre Etat, ou à cause de tout autre rapport avec ces sociétés; mais les produits distribués par ces dernières sociétés et passibles de l'impôt sont, le cas échéant, augmentés de tous les béné-

fices ou avantages que la société du premier Etat aurait indirectement retiré desdites sociétés, soit par voie de majoration ou de diminution des prix d'achat ou de vente, soit par tout autre moyen.

Article 15

1. Lorsqu'une société ayant son domicile fiscal dans l'un des Etats contractants s'y trouve soumise au payement d'un impôt frappant les distributions de revenus de valeurs mobilières et de revenus assimilés et qu'elle possède un ou plusieurs établissements stables sur le territoire d'un ou de plusieurs Etats contractants à raison desquels elle est également soumise dans ces derniers Etats au payement d'un même impôt, il est procédé à une répartition, entre les divers Etats intéressés, des revenus donnant ouverture audit impôt, afin d'éviter une double imposition.

2. La répartition prévue au paragraphe qui précède s'établit, pour chaque exercice, sur la base du rapport:

$\frac{A}{B}$ pour l'Etat dans lequel la société n'a pas son domicile fiscal

$\frac{B-A}{B}$ pour l'Etat dans lequel la société a son domicile fiscal;

la lettre A désignant le montant des bénéfices réputés réalisés par la société dans l'ensemble de ses établissements stables situés dans l'Etat où elle n'a pas son domicile fiscal, au regard de la documentation et de la réglementation fiscales qui s'y trouvent applicables pour l'imposition desdits bénéfices, ainsi que des dispositions des articles 10 et 11;

la lettre B le bénéfice comptable total de la société, tel qu'il résulte de son bilan général.

Pour la détermination du bénéfice comptable total, il est fait abstraction des résultats de l'ensemble des établissements stables situés dans un Etat lorsque ces résultats sont déficitaires.

Dans le cas où le bénéfice comptable total d'un exercice est nul ou négatif, la répartition s'effectue sur les bases antérieurement dégagées.

En l'absence de bases antérieurement dégagées, la répartition s'effectue selon une quotité fixée par commune entente entre les autorités compétentes des Etats contractants intéressés.

Article 16

1. Quant à la suite de contrôles exercés par les administrations fiscales compétentes, il est effectué sur le montant des bénéfices réalisés au cours d'un exercice, des redressements ayant pour résultat de modifier la proportion définie au paragraphe 2 de l'article 15, il est tenu compte de ces redressements pour la répartition: entre les Etats contractants intéressés, des bases d'imposition afférentes à l'exercice au cours duquel les redressements interviennent.

2. Les redressements portant sur le montant des revenus à répartir, mais n'affectant pas la proportion des bénéfices réalisés dont il a été tenu compte pour la répartition des revenus faisant l'objet desdits redressements, donnent lieu, selon les règles applicables dans chaque Etat, à une imposition supplémentaire répartie suivant la même proportion que l'imposition initiale.

Article 17

1. La répartition des bases d'imposition visée à l'article 15 et opérée par la société et notifiée par elle à chacune des administrations fiscales compétentes, dans le

délai qui lui est imparti par la législation de chaque Etat, pour déclarer des distributions de produits imposables auxquelles elle procède.

A l'appui de cette répartition, la société fournit à chacune desdites administrations, en outre des documents qu'elle est tenue de produire ou de déposer en vertu de la législation interne, une copie de ceux produits ou déposés auprès de l'administration des autres Etats.

2. Les difficultés ou contestations qui peuvent surgir au sujet de la répartition des bases d'imposition sont réglées d'une commune entente entre les administrations fiscales compétentes.

A défaut d'accord, le différend est tranché par la commission mixte prévue à l'article 41.

Article 18

Les tantièmes, jetons de présence et autres rémunérations attribués aux membres des conseils d'administration ou de surveillance des sociétés anonymes, sociétés en commandite par actions ou sociétés coopératives, en leur dite qualité, sont imposables dans l'Etat contractant où la société a son domicile fiscal, sous réserve de l'application des articles 22 et 23 ci-après en ce qui concerne les rémunérations perçues par les intéressés en leurs autres qualités effectives.

Si la société possède un ou plusieurs établissements stables sur le territoire d'un ou de plusieurs autres Etats contractants, les tantièmes, jetons de présence et autres rémunérations visés ci-dessus sont imposés dans les conditions fixées aux articles 15 à 17.

Article 19

1. L'impôt sur le revenu des prêts, dépôts, comptes de dépôts, bons de caisse et de toutes autres créances non représentées par des titres négociables est perçu dans l'Etat du domicile fiscal du créancier.

Toutefois, si le créancier domicilié dans l'un des Etats contractants possède un établissement stable dans un autre Etat contractant et si cet établissement consent un prêt ou effectue un dépôt, l'impôt est perçu dans ce dernier Etat.

2. Chaque Etat contractant conserve le droit d'imposer par voie de retenue à la source, si sa législation interne le prévoit les revenus visés au paragraphe I ci-dessus, à moins qu'il ne soit justifié, selon les modalités qui seront fixées d'une commune entente entre les autorités compétentes, que le bénéficiaire des revenus a son domicile fiscal dans un autre Etat contractant et que lesdits revenus y sont imposables.

Article 20

1. Les redevances (royalties) versées par la jouissance des biens immobiliers ou l'exploitation de mines, carrières ou autres ressources naturelles sont imposables dans celui des Etats contractants où sont situés ces biens, mines, carrières ou autres ressources naturelles.

2. Les droits d'auteur ainsi que les produits ou redevances (royalties) provenant de la vente ou de la concession de licences d'exploitation de brevets, marques de fabrique, procédés et formules secrets qui sont payés dans l'un des Etats contractants à une personne ayant son domicile fiscal dans un autre Etat contractant sont exonérés d'impôt dans le premier Etat.

3. Sont traitées comme les redevances visées au paragraphe 2, les sommes payées par la location ou le droit d'utilisation des

films cinématographiques, les droits de location et rémunérations analogues pour l'usage ou le droit à usage d'équipements industriels, commerciaux ou scientifiques et pour la fourniture d'informations concernant des expériences d'ordre industriel, commercial ou scientifique.

4. Si une redevance (royalty) est supérieure à la valeur intrinsèque et normale des droits pour lesquels elle est payée, l'exemption prévue aux paragraphes 2 et 3 ne peut être appliquée qu'à la partie de cette redevance qui correspond à cette valeur intrinsèque et normale.

5. Les dispositions des paragraphes 2 et 3 ne s'appliquent pas lorsque le bénéficiaire des redevances ou autres rémunérations entretient dans l'Etat contractant d'où proviennent ces revenus un établissement stable ou une installation fixe d'affaires servant à l'exercice d'une profession libérale ou d'une autre activité indépendante et que ces redevances ou autres rémunérations sont à attribuer à cet établissement stable ou à cette installation fixe d'affaires. Dans ce cas, ledit Etat a le droit d'imposer ces revenus conformément à sa législation.

Article 21

Les pensions et les rentes viagères sont imposables à l'impôt cédulaire ou tout impôt équivalent, dans l'Etat contractant où le bénéficiaire a son domicile fiscal.

Article 22

1. Sauf accords particuliers prévoyant des régimes spéciaux en cette matière, les salaires, traitements et autres rémunérations similaires qu'une personne domiciliée dans un Etat contractant reçoit au titre d'un emploi salarié ne sont imposables à l'impôt cédulaire ou tout impôt équivalent que dans cet Etat, à moins que l'emploi ne soit exercé dans un autre Etat contractant. Si l'emploi est exercé dans un autre Etat contractant, les rémunérations reçues à ce titre sont imposables dans cet autre Etat.

2. Nonobstant les dispositions précédentes du présent article, les rémunérations afférentes à une activité exercée à bord d'un navire ou d'un aéronef en trafic international sont imposables dans l'Etat contractant où l'entreprise a son domicile.

Article 23

1. Les revenus qu'une personne domiciliée dans un Etat contractant retire d'une profession libérale ou d'autres activités indépendantes de caractère analogue sont imposables dans cet Etat, à moins que cette personne ne dispose de façon habituelle dans d'autres Etats contractants de bases fixes pour l'exercice de ses activités. Si elle dispose de telles bases, la partie des revenus qui peut être attribuée à chacune d'elles est imposable dans l'Etat où elle est située.

2. Sont considérées comme professions libérales au sens du présent article, notamment l'activité scientifique, artistique, littéraire, enseignante ou pédagogique ainsi que celle des médecins, avocats, architectes ou ingénieurs.

Article 24

Les sommes qu'un étudiant ou un stagiaire de l'un des Etats contractants, séjournant dans un autre Etat contractant à seule fin d'y poursuivre ses études ou sa formation, reçoit pour couvrir les frais d'entretien, d'études ou de formation ne sont pas imposables dans cet autre Etat, à condition qu'elles proviennent de sources situées en dehors de cet autre Etat.

Article 25

Les revenus non mentionnés aux articles précédents sont imposables dans l'Etat contractant du domicile fiscal du bénéficiaire à moins que ces revenus ne se rattachent à l'activité d'un établissement stable que ce bénéficiaire possèderait dans un autre Etat contractant.

Article 26

Les contribuables qui transfèrent leur domicile en cours d'année d'un des Etats contractants à un autre Etat contractant sont imposés dans le premier Etat à un impôt général sur le revenu, acquis entre le premier janvier et la date du transfer de domicile, selon le tarif annuel.

Ils sont imposés au 1er janvier de l'année suivante dans l'Etat où ils ont transféré leur domicile sur le revenu acquis à compter de la date de ce transfert.

Les mêmes dispositions s'appliqueront en cas de plusieurs transferts de domicile en cours d'année.

CHAPITRE II

Impôts sur les successions

Article 27

1. Le présent chapitre est applicable aux impôts sur les successions perçus pour le compte de chacun des Etats contractants.

Sont considérés comme impôts sur les successions les impôts perçus par suite du décès sous forme d'impôts sur la masse successorale, d'impôts sur les parts héréditaires, de droits de mutation, ou d'impôts sur les donations pour cause de mort.

2. Les impôts actuels auxquels s'applique le présent chapitre dans chacun des Etats contractants sont énumérés au protocole annexé à la présente convention.

Article 28

Les biens immobiliers (y compris les accessoires) ne sont soumis à l'impôt sur les successions que dans l'Etat contractant où ils sont situés; le cheptel mort ou vif servant à une exploitation agricole ou forestière n'est imposable que dans l'Etat contractant où l'exploitation est située.

Article 29

Les biens meubles corporels ou incorporels laissés par un défunt ayant eu au moment de son décès son domicile dans l'un des Etats contractants et investis dans une entreprise commerciale, industrielle ou artisanale de tout genre seront soumis à l'impôt sur les successions suivant la règle ci-après:

a) si l'entreprise ne possède un établissement stable que dans l'un des Etats contractants, les biens ne seront soumis à l'impôt que dans cet Etat; il en est ainsi même lorsque l'entreprise étend son activité sur le territoire des autres Etats contractants sans y avoir un établissement stable;

b) si l'entreprise a un établissement stable dans plusieurs Etats contractants, les biens seront soumis à l'impôt dans chaque Etat dans la mesure où ils sont affectés à un établissement stable situé sur le territoire de cet Etat.

Toutefois, les dispositions du présent article ne sont pas applicables aux investissements effectués par le défunt dans les sociétés à base de capitaux (sociétés anonymes, sociétés en commandite par actions, sociétés à responsabilité limitée, sociétés coopératives, sociétés civiles soumises au régime des sociétés de capitaux) ou sous forme de commandite dans les sociétés en commandite simple.

Article 30

Les biens meubles corporels ou incorporels rattachés à des installations permanentes et affectés à l'exercice d'une profession libérale dans l'un des Etats contractants ne sont soumis à l'impôt sur les successions que dans l'Etat contractant où se trouvent ces installations.

Article 31

Les biens meubles corporels, y compris les meubles meublants, le linge et les objets ménagers ainsi que les objets et collections d'art autres que les meubles visés aux articles 29 et 30 ne sont soumis à l'impôt sur les successions que dans celui des Etats contractants où ils se trouvent effectivement à la date du décès.

Toutefois les bateaux et les aéronefs ne sont imposables que dans l'Etat contractant où ils ont été immatriculés.

Article 32

Les biens de la succession auxquels les articles 28 à 31 ne sont pas applicables ne sont soumis aux impôts sur les successions que dans l'Etat contractant où le défunt avait son domicile au moment de son décès.

Article 33

1. Les dettes afférentes aux entreprises visées aux articles 29 et 30 seront imputables sur les biens affectés à ces entreprises. Si l'entreprise possède selon le cas un établissement stable ou une installation permanente dans plusieurs des Etats contractants, les dettes seront imputables sur les biens affectés à l'établissement ou à l'installation dont elles dépendent.

2. Les dettes garanties, soit par des immeubles ou des droits immobiliers, soit par des bateaux ou aéronefs visés à l'article 31, soit par des biens affectés à l'exercice d'une profession libérale dans les conditions prévues à l'article 30, soit par des biens affectés à une entreprise de la nature visée à l'article 29, seront imputables sur ces biens. Si la même dette est garantie à la fois par des biens situés dans plusieurs Etats, l'imputation se fera sur des biens situés dans chacun d'eux proportionnellement à la valeur taxable de ces biens.

Cette disposition n'est applicable aux dettes visées au paragraphe 1 que dans la mesure où ces dettes ne seront pas couvertes par l'imputation prévue à ce paragraphe.

3. Les dettes non visées aux paragraphes 1 et 2 seront imputées sur les biens auxquels sont applicables les dispositions de l'article 32.

4. Si l'imputation prévue aux trois paragraphes qui précèdent laisse subsister dans un Etat contractant un solde non couvert, ce solde sera déduit des autres biens soumis à l'impôt des successions dans ce même Etat. S'il ne reste pas dans cet Etat d'autres biens soumis à l'impôt ou si la déduction laisse encore un solde non couvert, ce solde sera imputé proportionnellement sur les biens soumis à l'impôt dans les autres Etats contractants.

Article 34

Nonobstant les dispositions des articles 28 à 33, chaque Etat contractant conserve le droit de calculer l'impôt sur les biens héréditaires qui sont réservés à son imposition exclusive, d'après le taux moyen qui serait applicable s'il était tenu compte de l'ensemble des biens qui seraient imposables d'après sa législation interne.

CHAPITRE III

Droits d'enregistrement autres que les droits de succession– Droits de timbre

Article 35

Lorsqu'un acte ou un jugement établi dans l'un des Etats contractants est présenté à l'enregistrement dans un autre Etat contractant, les droits applicables dans ce dernier Etat sont déterminés suivant les règles prévues par sa législation interne, sauf imputation, le cas échéant, des droits d'enregistrement qui auraient été perçus dans le premier Etat, sur les sommes ou valeurs donnant ouverture aux droits dans cet autre Etat.

Toutefois, les actes ou jugement portant mutation de propriété, d'usufruit d'immeubles ou de fonds de commerce, ceux portant mutation de jouissance d'immeubles et les actes ou jugements constatant une cession de droit à un bail ou au bénéfice d'une promesse de bail portant sur tout ou partie d'un immeuble ne peuvent être assujettis à un droit de mutation que dans celui des Etats contractants sur le territoire duquel ces immeubles ou ces fonds de commerce sont situés.

En outre, les dispositions des alinéas précédents ne sont pas applicables aux actes constitutifs de société ou modificatifs du pacte social.

Ces actes donnent lieu à la perception des droits proportionnels dans l'Etat où est situé le siège statutaire de la société. S'il s'agit de fusion ou d'opération assimilée, la perception est effectuée dans l'Etat où est situé le siège de la société absorbante ou nouvelle.

Article 36

Les actes ou effets créés dans l'un des Etats contractants ne sont pas soumis au timbre dans un autre Etat contractant lorsqu'ils ont effectivement supporté cet impôt au tarif applicable dans le premier Etat, ou lorsqu'ils en sont légalement exonérés dans ledit Etat.

TITRE III

ASSISTANCE ADMINISTRATIVE

Article 37

1. Les autorités fiscales de chacun des Etats contractants transmettent aux autorités fiscales des autres Etats contractants les renseignements d'ordre fiscal qu'elles ont à leur disposition et qui seraient utiles à ces dernières autorités pour assurer l'établissement et le recouvrement réguliers des impôts visés par la présente convention ainsi que l'application, en ce qui concerne ces impôts, des dispostions légales relatives à la répression de la fraude fiscale.

2. Les renseignements ainsi échangés qui conservent un caractère secret, ne sont pas communiqués à des personnes autres que celles qui sont chargées de l'assiette et du recouvrement des impôts visés par la présente convention. Aucun renseignement n'est échangé qui révèlerait un secret commercial, industriel ou professionnel. L'assistance peut ne pas être donnée lorsque l'Etat requis estime qu'elle est de nature à mettre en danger sa souveraineté ou sa sécurité ou à porter atteinte à ses intérêts généraux.

3. L'échange de renseignements a lieu soit d'office, soit sur demande visant des cas concrets. Les autorités compétentes des Etats contractants s'entendent pour déterminer la liste des informations qui sont fournies d'office.

Article 38

Les Etats contractants conviennent de se prêter mutuellement assistance et appui en vue de recouvrer, suivant des règles propres à leur législation ou réglementation respectives, les impôts visés par la présente convention ainsi que les majorations de droits, droits en sus, indemnités de retard, intérêts et frais afférents à ces impôts, lorsque ces sommes sont définitivement dûes en application des lois ou règlements de l'Etat demandeur.

2. La demande formulée à cette fin doit être accompagneé des documents exigés par les lois et réglements de l'Etat réquérant pour établir que les sommes à recouvrer sont définitivement dûes.

Au vu de ces documents, les significations, et mesures de recouvrement et de perception ont lieu dans l'Etat requis conformément aux lois ou règlements applicables pour le recouvrement et la perception de ses propres impôts.

4. Les créances fiscales à recouvrer bénéficient des mêmes sûretés et privilèges que les créances fiscales de même nature dans l'Etat de recouvrement.

Article 39

En ce qui concerne les créances fiscales qui sont encore susceptibles de recours, les autorités fiscales de l'Etat créancier, pour la sauvegarde de ses droits, peuvent demander aux autorités fiscales compétentes d'un autre Etat de prendre les mesures conservatoires que la législation ou la réglementation de celui-ci autorise.

Article 40

Les mesures d'assistance définies aux articles 38 et 39 s'appliquent également au recouvrement de tous impôts et taxes autres que ceux visés par la présente convention.

TITRE IV

DISPOSITIONS DIVERSES

Article 41

1. Tout contribuable qui prouve que les mesures prises par les autorités fiscales des Etats contractants ont entraîné pour lui une double imposition en ce qui concerne les impôts visés par la présente convention peut adresser une demande, soit aux autorités compétentes de l'Etat sur le territoire duquel il a son domicile fiscal, soit à celle de celui ou des autres Etats contractants qu'intéresse la question. Si le bien fondé de cette demande est reconnu, les autorités compétentes desdits Etats s'entendent pour éviter de façon équitable la double imposition.

2. Les autorités compétentes des Etats contractants peuvent également s'entendre pour supprimer la double imposition dans les cas non réglés par la présente convention, ainsi que dans les cas où l'interprétation ou l'application de la présente convention donnerait lieu à des difficultés ou à des doutes.

3. S'il apparaît que, pour parvenir à une entente, des pourparlers soient opportuns, l'affaire est déférée à une commission mixte composée de représentants dés Etats intéressés, désignés par les Ministres des Finances. La présidence de la commission est exercée successivement par un membre de chaque délégation.

Article 42

La présente convention sera sujette à ratification ou approbation et entrera en vigueur dès que les instruments de ratification ou d'approbation de tous les Etats signataires auront été échangés, étant entendu qu'elle produira ses effets.

– en ce qui concerne les impôts sur les revenus, pour l'imposition des revenus afférents à l'année 1963 ou aux exercices clos au cours de cette année. Toutefois, pour ce qui est des revenus dont l'imposition est réglée par les articles 15 à 18, la convention s'appliquera aux distributions qui auront lieu postérieurement à l'entrée en vigueur de la convention.

– en ce qui concerne les impôts sur les successions, pour les successions de personnes dont le décès se produira depuis et y compris le jour de l'entrée en vigueur de la convention;

– en ce qui concerne les autres droits d'enregistrement et les droits de timbre, pour les actes et les jugements postérieurs à l'entrée en vigueur de la convention.

Article 43

La convention restera en vigueur pendant une durée indéfinie.

Toutefois à partir du 1er Janvier 1967, le Gouvernement de chaque Etat contractant pourra, jusqu'au 30 juin de chaque année, notifier aux autres Etats l'intention de mettre fin aux effets de la convention. En ce cas, la convention cessera de s'appliquer, à l'Etat considéré, à partir du 1er janvier de l'année suivant la date de la notification, étant entendu que les effets en seront limités:

– en ce qui concerne l'imposition des revenus, aux revenus acquis ou mis en paiement dans l'année au cours de laquelle la notification sera intervenue;

– en ce qui concerne l'imposition des successions, aux successions ouvertes au plus tard le 31 décembre de ladite année;

– en ce qui concerne les autres droits d'enregistrement et les droits de timbre, aux actes et aux jugements intervenus au plus tard le 31 décembre de ladite année;

En foi de quoi les plénipotentiaires soussignés dûment autorisés à cet effet, ont signé la présente convention et y ont apposé leur sceau.

Fait à le

en autant d'exemplaires originaux que de Hautes Parties Contractantes.

Abkommen zwischen der Bundesrepublik Deutschland und der Argentinischen Republik zur Vermeidung der Doppelbesteuerung auf dem Gebiete der Steuern vom Einkommen und vom Vermögen

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EINLEITUNG

Das deutsch-argentinische Abkommen vom 13. Juli 1966 ist das erste deutsche Doppelbesteuerungsabkommen mit einem südamerikanischen Staat.

Die Verhandlungen über den Abschluss eines Doppelbesteuerungsabkommens mit Brasilien sind durch erste Gespräche eingeleitet und werden voraussichtlich in Kürze fortgesetzt und abgeschlossen werden. Verhandlungen mit Chile, Ekuador und Kolombien sind in Aussicht genommen. Das heutzutage ziemlich kleine Netz südamerikanischer Doppelbesteuerungsabkommen dehnt sich also weiter aus[1]). Die Abkommen sind insoweit für das internationale Steuerrecht von besonderer Bedeutung als sie zwischen dem Prinzip der Welteinkommenbesteuerung und dem Territorialprinzip einen Ausgleich bewirken. Das Prinzip der Welteinkommenbesteuerung ist u.a. in den europäischen Steuergesetzen verankert; in den südamerikanischen Systemen wird nicht nur bei der indirekten Besteuerung, sondern auch bei der direkten Besteuerung das Territorialprinzip befolgt[2]).

Die schwierige Aufgabe einen Ausgleich zu der in Argentinien geltenden Territorialbesteuerung zu schaffen hat, wie Dr. Debatin[3]) bemerkt, eine relativ weitgehende Abweichung von dem O.E.C.D. Musterabkommen unvermeidlich gemacht.

1) vgl. Bulletin 1966, S. 163 ff., D.B.A. Brasilien.
2) vgl. "Corporations and Taxation in Argentina" in dieser Nummer des Bulletins, S. 99 ff.
3) vgl. Dr. H. Debatin, Das internationale Steuerrecht in der Entwicklung, Deutsche Steuer Zeitung, Ausgabe A, 1967, Nr. 1, S. 9 ff.

Das vorliegende deutsch-argentinische Abkommen folgt trotzdem in zahlreichen Bestimmungen dem von der O.E.C.D. empfohlenen Muster für Doppelbesteuerungsabkommen. Wie in der deutschen Denkschrift zum Abkommen bemerkt wird, kann für die Auslegung dieser Bestimmungen der Kommentar zum Musterabkommen der O.E.C.D. herangezogen werden[4]). Dies trägt zur Vereinheitlichung des internationalen Steuerrechts bei.

Nach der üblichen deutschen Vertragspraxis sind im deutsch-argentinischen Doppelbesteuerungsabkommen Einkünfte, mit denen sich das Abkommen befasst und die nach dem Abkommen in Argentinien steuerbar sind, von den deutschen Steuern befreit. Ein Beispiel bilden die Einkünfte aus Betriebstätten. Diese Freistellungsmethode führt jedoch nicht so weit, dass die befreiten Einkünfte bei der Ermittlung des Steuersatzes für die übrigen Einkünfte ausscheiden. Es besteht also der Progressionsvorbehalt.

Nicht die obenerwähnte Freistellungsmethode, sondern die Anrechnungsmethode gilt für Dividenden — ausser für die aus wesentlichen Beteiligungen[5]) — Zinsen, Lizenzgebühren und Aufsichts- und Verwaltungsratsvergütungen, die in Argentinien zwar der Quellensteuer unterliegen, jedoch zur Besteuerung der Bundesrepublik Deutschland zugewiesen sind. Das Abkommen fördert nun die entwicklungspolitisch erwünschten deutschen Privatinvestionen in Argentinien dadurch, dass bei der Festsetzung der Anrechnungsbeträge berücksichtigt wird, dass das argentinische Steuerrecht in gewissen Fällen Anreize für ausländische Investionen schafft, z.B. indem es für ins Ausland fliessende Einkünfte gezielte Steuerbefreiungen gewährt. Die deutsche Besteuerung würde solche Anreize beseitigen, wenn auf die volle deutsche Steuer von diesen Einkünften nur die tatsächlich gezahlte argentinische Steuer angerechnet würde. Das vorliegende Abkommen beschränkt in gewissen Fällen die steuerliche Anreize beseitigenden Auswirkungen der Anrechnungsmethode und zwar dadurch, dass es eine fiktive Steueranrechnung vorschreibt'[6]). Die deutsche Steuer wird also gekürzt, obwohl der Steuerpflichtige die argentinische Steuer tatsächlich nicht oder nicht voll entrichtet hat. Der Steuervorteil in Argentinien geht also nicht verloren.

Das Abkommen bedarf der Ratifikation; die Ratifikationsurkunden sind noch nicht ausgetauscht worden. Das Abkommen tritt, Art. 27 des Abkommens gemäss, einen Monat nach Austausch der Ratifikationsurkunden in Kraft, und gilt dann für die Steuern, die erhoben werden für das dem Jahre des Austausches der Ratifikationsurkunden folgende Kalenderjahr, sowie für die darauf folgenden Kalenderjahre. Das Abkommen wird also nicht eher Anwendung finden können als für die Steuern, die für 1968 erhoben werden[7]).

4) Deutscher Bundestag – 5. Wahlperiode, Drucksache V/1087.

5) Indem das Abkommen die Freistellung auch für Dividenden aus wesentlichen Beteiligungen deutscher an argentinischen Kapitalgesellschaften sowie für solche Beteiligungen selbst, gewährt, weitet es – der deutschen Vertragspraxis entsprechend –, das deutsche Schachtelprivileg über die Grenze aus.

6) vgl. Art. 20, Abs. 1, b.

7) Die betreffenden Daten werden in "Tax News Service" veröffentlicht worden als bald als sie bekannt sind.
Der Deutsche Bundestag und der Deutsche Bundesrat haben dem Abkommen zugestimmt (Gesetz vom 18. Februar 1967, Bundesgesetzblatt II, 25. Februar 1967).

Text

des Abkommens zwischen der Bundesrepublik Deutschland und der Argentinischen Republik zur Vermeidung der Doppelbesteuerung auf dem Gebiete der Steuern vom Einkommen und vom Vermögen vom 13. Juli 1966

DIE BUNDESREPUBLIK DEUTSCHLAND
UND
DIE ARGENTINISCHE REPUBLIK,

VON DEM WUNSCHE GELEITET, ein Abkommen zur Vermeidung der Doppelbesteuerung auf dem Gebiete der Steuern vom Einkommen und vom Vermögen zu schließen,

HABEN FOLGENDES VEREINBART:

Artikel 1

Dieses Abkommen gilt für Personen, die in einem Vertragstaat oder in beiden Vertragstaaten ansässig sind.

Artikel 2

(1) Die Steuern, für die dieses Abkommen gilt, sind

1. in der Bundesrepublik Deutschland:
   a) die Einkommensteuer,
   b) die Körperschaftsteuer,
   c) die Vermögensteuer,
   d) die Gewerbesteuer,
   (im folgenden als „deutsche Steuer" bezeichnet);
2. in der Argentinischen Republik:
   a) die Einkommensteuer (impuesto a los réditos),
   b) die Vermögenszuwachssteuer (impuesto a las ganancias eventuales),
   c) die Notsteuer (impuesto de emergencia),
   (im folgenden als „argentinische Steuer" bezeichnet).

(2) Das Abkommen gilt auch für alle Steuern gleicher oder ähnlicher Art, die künftig neben den zur Zeit bestehenden Steuern oder an deren Stelle erhoben werden.

(3) Die Bestimmungen dieses Abkommens über die Besteuerung des Einkommens oder des Gewinns gelten entsprechend für die nicht nach dem Einkommen oder dem Vermögen berechnete deutsche Gewerbesteuer.

Artikel 3

(1) Im Sinne dieses Abkommens, wenn der Zusammenhang nichts anderes erfordert:

a) bedeutet der Ausdruck „Bundesrepublik" die Bundesrepublik Deutschland, und, im geographischen Sinne verwendet, den Geltungsbereich des Grundgesetzes für die Bundesrepublik Deutschland;
b) bedeutet der Ausdruck „Argentinien" die Argentinische Republik;
c) bedeuten die Ausdrücke „ein Vertragstaat" und „der andere Vertragstaat", je nach dem Zusammenhang, die Bundesrepublik oder Argentinien;
d) umfaßt der Ausdruck „Person" natürliche Personen und Gesellschaften;
e) bedeutet der Ausdruck „Gesellschaft" juristische Personen oder Rechtsträger, die für die Besteuerung wie juristische Personen behandelt werden;
f) bedeuten die Ausdrücke „Unternehmen eines Vertragstaates" und „Un-

ternehmen des anderen Vertragstaates", je nachdem, ein Unternehmen, das von einer in einem Vertragstaat ansässigen Person betrieben wird, oder ein Unternehmen, das von einer in dem anderen Vertragstaat ansässigen Person betrieben wird;

g) bedeutet der Ausdruck „zuständige Behörde" auf seiten der Bundesrepublik den Bundesminister der Finanzen und auf seiten Argentiniens den Secretario de Estado de Hacienda.

(2) Bei Anwendung dieses Abkommens durch einen Vertragstaat hat, wenn der Zusammenhang nichts anderes erfordert, jeder in diesem Abkommen nicht anders definierte Ausdruck die Bedeutung, die ihm nach dem Recht dieses Staates über die Steuern zukommt, für die dieses Abkommen gilt.

Artikel 4

(1) Im Sinne dieses Abkommens bedeutet der Ausdruck „eine in einem Vertragstaat ansässige Person" eine Person, die ihren Wohnsitz, ihren ständigen Aufenthalt, ihren gewöhnlichen Aufenthalt, den Ort ihrer Geschäftsleitung oder ihren Sitz in diesem Staate hat.

(2) Ist nach Absatz 1 eine natürliche Person in beiden Vertragstaaten ansässig, so gilt folgendes:

a) Die Person gilt als in dem Vertragstaat ansässig, in dem sie über eine ständige Wohnstätte verfügt. Verfügt sie in beiden Vertragstaaten über eine ständige Wohnstätte, so gilt sie als in dem Vertragstaat ansässig, zu dem sie die engeren persönlichen und wirtschaftlichen Beziehungen hat (Mittelpunkt der Lebensinteressen).

b) Kann nicht bestimmt werden, in welchem Vertragstaat die Person den Mittelpunkt der Lebensinteressen hat, oder verfügt sie in keinem der Vertragstaaten über eine ständige Wohnstätte, so gilt sie als in dem Vertragstaat ansässig, in dem sie ihren gewöhnlichen Aufenthalt hat.

c) Hat die Person ihren gewöhnlichen Aufenthalt in beiden Vertragstaaten oder in keinem der Vertragstaaten, so regeln die zuständigen Behörden der Vertragstaaten die Frage in gegenseitigem Einvernehmen.

(3) Ist nach Absatz 1 eine Gesellschaft in beiden Vertragstaaten ansässig, so gilt sie als in dem Vertragstaat ansässig, in dem sich der Ort ihrer tatsächlichen Geschäftsleitung befindet.

Artikel 5

(1) Im Sinne dieses Abkommens bedeutet der Ausdruck „Betriebstätte" eine feste Geschäftseinrichtung, in der die Tätigkeit des Unternehmens ganz oder teilweise ausgeübt wird.

(2) Der Ausdruck „Betriebstätte" umfaßt insbesondere:

a) einen Ort der Leitung,
b) eine Zweigniederlassung,
c) eine Geschäftsstelle,
d) eine Fabrikationsstätte,
e) eine Werkstätte,
f) ein Bergwerk, einen Steinbruch oder eine andere Stätte der Ausbeutung von Bodenschätzen,
g) eine Bauausführung oder Montage, deren Dauer sechs Monate überschreitet.

(3) Als Betriebstätten gelten nicht:

a) Einrichtungen, die ausschließlich zur Lagerung, Ausstellung oder Auslieferung von Gütern oder Waren des Unternehmens benutzt werden;

b) Bestände von Gütern oder Waren des Unternehmens, die ausschließlich zur Lagerung, Ausstellung oder Auslieferung unterhalten werden;
c) Bestände von Gütern oder Waren des Unternehmens, die ausschließlich zu dem Zweck unterhalten werden, durch ein anderes Unternehmen bearbeitet oder verarbeitet zu werden;
d) eine feste Geschäftseinrichtung, die ausschließlich zu dem Zweck unterhalten wird, für das Unternehmen Güter oder Waren einzukaufen oder Informationen zu beschaffen;
e) eine feste Geschäftseinrichtung die ausschließlich zu dem Zweck unterhalten wird, für das Unternehmen zu werben, Informationen zu erteilen, wissenschaftliche Forschung zu betreiben oder ähnliche Tätigkeiten auszuüben, die vorbereitender Art sind oder eine Hilfstätigkeit darstellen.

(4) Ein Unternehmen eines Vertragstaates wird so behandelt, als habe es eine Betriebstätte in dem anderen Vertragstaat, wenn es in dem letztgenannten Staat nicht nur gelegentlich Verträge durch eine oder mehrere Personen — mit Ausnahme von unabhängigen Vertretern im Sinne des Absatzes 5 — schließt, die bevollmächtigt sind, solche Verträge im Namen des Unternehmens zu schließen, es sei denn, daß diese Verträge den Einkauf von Gütern und Waren für das Unternehmen zum Gegenstand haben.

(5) Ein Unternehmen eines Vertragstaates wird nicht schon deshalb so behandelt, als habe es eine Betriebstätte in dem anderen Vertragstaat, weil es dort seine Tätigkeit durch einen Makler, Kommissionär oder einen anderen unabhängigen Vertreter ausübt, sofern diese Personen im Rahmen ihrer ordentlichen Geschäftstätigkeit handeln.

(6) Allein dadurch, daß eine in einem Vertragstaat ansässige Gesellschaft eine Gesellschaft beherrst oder von einer Gesellschaft beherrscht wird, die in dem anderen Vertragstaat ansässig ist oder dort (entweder durch eine Betriebstätte oder in anderer Weise) ihre Tätigkeit ausübt, wird eine der beiden Gesellschaften nicht zur Betriebstätte der anderen.

(7) Ungeachtet des Absatzes 3 Buchstabe d und des Absatzes 4 wird ein Unternehmen eines Vertragstaates so behandelt, als habe es eine Betriebstätte in dem anderen Vertragstaat, wenn das Unternehmen in dem anderen Staat eine feste Geschäftseinrichtung oder einen Vertreter im Sinne des Absatzes 4 für den Einkauf von Erzeugnissen der Landwirtschaft oder Viehzucht hat.

Artikel 6

(1) Einkünfte aus unbeweglichem Vermögen können in dem Vertragstaat besteuert werden, in dem dieses Vermögen liegt.

(2) Der Ausdruck „unbewegliches Vermögen" bestimmt sich nach dem Recht des Vertragstaates, in dem das Vermögen liegt. Der Ausdruck umfaßt in jedem Fall das Zubehör zum unbeweglichen Vermögen, das lebende und tote Inventar land- und forstwirtschaftlicher Betriebe, die Rechte, auf die die Vorschriften des Privatrechts über Grundstücke Anwendung finden, die Nutzrechte an unbeweglichem Vermögen sowie die Rechte auf veränderliche oder feste Vergütung für die Ausbeutung oder das Recht auf Ausbeutung von Mineralvorkommen, Quellen und anderen Bodenschätzen; Schiffe und Luftfahrzeuge gelten nicht als unbewegliches Vermögen.

(3) Absatz 1 gilt für Einkünfte aus der unmittelbaren Nutzung, der Vermietung

oder Verpachtung sowie jeder anderen Art der Nutzung unbeweglichen Vermögens.

(4) Die Absätze 1 und 3 gelten auch für die Einkünfte aus unbeweglichem Vermögen eines Unternehmens und für Einkünfte aus unbeweglichem Vermögen, das der Ausübung eines freien Berufes dient.

Artikel 7

(1) Gewinne eines Unternehmens eines Vertragstaates können nur in diesem Staat besteuert werden, es sei denn, daß das Unternehmen seine Tätigkeit im anderen Vertragstaat durch eine dort gelegene Betriebstätte ausübt. Übt das Unternehmen seine Tätigkeit in dieser Weise aus, so können die Gewinne des Unternehmens in dem anderen Staat besteuert werden, jedoch nur insoweit, als sie dieser Betriebstätte zugerechnet werden können.

(2) Übt ein Unternehmen eines Vertragstaates seine Tätigkeit in dem anderen Vertragstaat durch eine dort gelegene Betriebstätte aus, so sind in jedem Vertragstaat dieser Betriebstätte die Gewinne zuzurechnen, die sie hätte erzielen können, wenn sie eine gleiche oder ähnliche Tätigkeit unter gleichen oder ähnlichen Bedingungen als selbständiges Unternehmen ausgeübt hätte und im Verkehr mit dem Unternehmen, dessen Betriebstätte sie ist, völlig unabhängig gewesen wäre.

(3) Bei der Ermittlung der Gewinne einer Betriebstätte werden die für diese Betriebstätte entstandenen Aufwendungen, einschließlich der Geschäftsführungs- und allgemeinen Verwaltungskosten, zum Abzug zugelassen, gleichgültig, ob sie in dem Staat, in dem die Betriebstätte liegt, oder anderswo entstanden sind.

(4) Außer in den Fällen des Artikels 5 Absatz 7 wird auf Grund des bloßen Einkaufs von Gütern oder Waren für das Unternehmen einer Betriebstätte kein Gewinn zugerechnet.

(5) Gehören zu den Gewinnen Einkünfte, die in anderen Artikeln dieses Abkommens behandelt werden, so werden die Bestimmungen dieses Artikels nicht berührt.

Artikel 8

(1) Gewinne aus dem Betrieb von Seeschiffen oder Luftfahrzeugen im internationalen Verkehr können nur in dem Vertragstaat besteuert werden, in dem sich der Ort der tatsächlichen Geschäftsleitung des Unternehmens befindet.

(2) Absatz 1 gilt entsprechend für Gewinne aus Beteiligungen dieser Unternehmen an einem Pool oder an einer Betriebsgemeinschaft der Seeschiffahrt oder Luftfahrt.

(3) Befindet sich der Ort der tatsächlichen Geschäftsleitung eines Unternehmens der Seeschiffahrt an Bord eines Schiffes, so gilt er als in dem Vertragstaat gelegen, in dem der Heimathafen des Schiffes liegt, oder, wenn kein Heimathafen vorhanden ist, in dem Vertragstaat, in dem die Person, die das Schiff betreibt, ansässig ist.

(4) Seeschiffe oder Luftfahrzeuge, die ein deutsches Unternehmen im internationalen Verkehr betreibt und die nicht in einem argentinischen Hafen registriert sind, gelten für die Zwecke der in Argentinien erhobenen Ersatzsteuer für unentgeltliche Vermögensübertragungen (Impuesto Sustitutivo a la Transmisión Gratuita de Bienes) nicht als Teil des Vermögens, das einer in Argentinien gelegenen Betriebstätte dieses Unternehmens zuzurechnen ist.

Artikel 9

Wenn

a) ein Unternehmen eines Vertrag-

staates unmittelbar oder mittelbar an der Geschäftsleitung, der Kontrolle oder am Kapital eines Unternehmens des anderen Vertragstaates beteiligt ist, oder

b) dieselben Personen unmittelbar oder mittelbar an der Geschäftsleitung, der Kontrolle oder am Kapital eines Unternehmens eines Vertragstaates und eines Unternehmens des anderen Vertragstaates beteiligt sind,

und in diesen Fällen zwischen den beiden Unternehmen hinsichtlich ihrer kaufmännischen oder finanziellen Beziehungen Bedingungen vereinbart oder auferlegt werden, die von denen abweichen, die unabhängige Unternehmen miteinander vereinbaren würden, so dürfen die Gewinne, die eines der Unternehmen ohne diese Bedingungen erzielt hätte, wegen dieser Bedingungen aber nicht erzielt hat, den Gewinnen dieses Unternehmens zugerechnet und entsprechend besteuert werden.

Artikel 10

(1) Dividenden, die eine in einem Vertragstaat ansässige Gesellschaft an eine in dem anderen Vertragstaat ansässige Person zahlt, können in dem erstgenannten Staat besteuert werden; die Steuer darf aber 15 vom Hundert des Bruttobetrages der Dividenden nicht übersteigen.

(2) Ungeachtet des Absatzes 1 darf die Steuer des erstgenannten Vertragstaates 15 vom Hundert, nicht aber 25 vom Hundert des Bruttobetrages der Dividenden übersteigen, wenn

a) dieser Staat die Körperschaftsteuer von ausgeschütteten Gewinnen zu einem niedrigeren Vomhundertsatz als von nichtausgeschütteten Gewinnen erhebt und der Unterschied zwischen diesen beiden Sätzen 20 Punkte oder mehr beträgt, und

b) die Dividenden von einer in diesem Staat ansässigen Gesellschaft an eine in dem anderen Staat ansässige Gesellschaft gezahlt werden, der mindestens 25 vom Hundert der stimmberechtigten Anteile der erstgenannten Gesellschaft gehören.

(3) Der in diesem Artikel verwendete Ausdruck „Dividenden" bedeutet Einkünfte aus Aktien oder anderen Rechten — ausgenommen Forderungen — mit Gewinnbeteiligung sowie aus sonstigen Gesellschaftsanteilen stammende Einkünfte, die nach dem Steuerrecht des Staates, in dem die ausschüttende Gesellschaft ansässig ist, den Einkünften aus Aktien gleichgestellt sind; er umfaßt auch Ausschüttungen auf Anteilscheine, die von Kapitalanlagegesellschaften ausgegeben worden sind und in der Bundesrepublik auch die Einkünfte, die ein stiller Gesellschafter aus seiner Beteiligung als stiller Gesellschafter bezieht.

(4) Die Absätze 1 und 2 sind nicht anzuwenden, wenn der in einem Vertragstaat ansässige Empfänger der Dividenden in dem anderen Vertragstaat, in dem die die Dividenden zahlende Gesellschaft ansässig ist, eine Betriebstätte hat und die Beteiligung, für die die Dividenden gezahlt werden, tatsächlich zu dieser Betriebstätte gehört. In diesem Fall ist Artikel 7 anzuwenden.

(5) Bezieht eine in einem Vertragstaat ansässige Gesellschaft Gewinne oder Einkünfte aus dem anderen Vertragstaat, so darf dieser andere Staat weder die Dividenden besteuern, die die Gesellschaft an nicht in diesem anderen Staat ansässige Personen zahlt, noch Gewinne der Gesellschaft einer Steuer für nicht ausgeschüttete Gewinne unterwerfen, selbst wenn die gezahlten Dividenden oder die

nicht ausgeschütteten Gewinne ganz oder teilweise aus in dem anderen Staat erzielten Gewinnen oder Einkünften bestehen.

Artikel 11

(1) Zinsen, die aus einem Vertragstaat stammen und an eine in dem anderen Vertragstaat ansässige Person gezahlt werden, können in dem erstgenannten Staat besteuert werden; die Steuer darf aber 20 vom Hundert des Bruttobetrages der Zinsen nicht übersteigen.

(2) Ungeachtet des Absatzes 1 sind

a) Zinsen, die aus Argentinien stammen und an die Deutsche Bundesbank oder an die Kreditanstalt für Wiederaufbau gezahlt werden, von der argentinischen Steuer befreit;

b) Zinsen, die aus der Bundesrepublik stammen und an die Zentralbank der Argentinischen Republik (Banco Central de la República Argentina) gezahlt werden, von der deutschen Steuer befreit.

(3) Der in diesem Artikel verwendete Ausdruck „Zinsen" bedeutet Einkünfte aus öffentlichen Anleihen, aus Schuldverschreibungen, auch wenn sie durch Pfandrechte an Grundstücken gesichert oder mit einer Gewinnbeteiligung ausgestattet sind, und aus Forderungen jeder Art sowie alle anderen Einkünfte, die nach dem Steuerrecht des Staates, aus dem sie stammen, den Einkünften aus Darlehen gleichgestellt sind.

(4) Die Absätze 1 und 2 sind nicht anzuwenden, wenn der in einem Vertragstaat ansässige Empfänger der Zinsen in dem anderen Vertragstaat, aus dem die Zinsen stammen, eine Betriebstätte hat und die Forderung, für die die Zinsen gezahlt werden, tatsächlich zu dieser Betriebstätte gehört. In diesem Fall ist Artikel 7 anzuwenden.

(5) Zinsen gelten dann als aus einem Vertragstaat stammend, wenn der Schuldner dieser Staat selbst, eines seiner Länder, eine seiner Gebietskörperschaften oder eine in diesem Staat ansässige Person ist. Hat aber der Schuldner der Zinsen, ohne Rücksicht darauf, ob er in einem Vertragstaat ansässig ist oder nicht, in einem Vertragstaat eine Betriebstätte und ist die Schuld, für die die Zinsen gezahlt werden, für Zwecke der Betriebstätte eingegangen worden und trägt die Betriebstätte die Zinsen, so gelten die Zinsen als aus dem Vertragstaat stammend, in dem die Betriebstätte liegt.

(6) Bestehen zwischen Schuldner und Gläubiger oder zwischen jedem von ihnen und einem Dritten besondere Beziehungen und übersteigen deshalb die gezahlten Zinsen, gemessen an der zugrunde liegenden Forderung, den Betrag, den Schuldner und Gläubiger ohne diese Beziehungen vereinbart hätten, so wird dieser Artikel nur auf diesen letzten Betrag angewendet. In diesem Fall kann der übersteigende Betrag nach dem Recht jedes Vertragstaates und unter Berücksichtigung der anderen Bestimmungen dieses Abkommens besteuert werden.

Artikel 12

(1) Lizenzgebühren, die aus einem Vertragstaat stammen und an eine in dem anderen Vertragstaat ansässige Person gezahlt werden, können in dem erstgenannten Staat besteuert werden; die Steuer darf aber 15 vom Hundert des Bruttobetrags der Lizenzgebühren nicht übersteigen.

(2) Der in diesem Artikel verwendete Ausdruck „Lizenzgebühren" bedeutet Vergütungen jeder Art, die für die Benutzung oder für das Recht auf Benutzung von Urheberrechten an literarischen, künst-

lerischen oder wissenschaftlichen Werken, einschließlich kinematographischer Filme, von Patenten, Warenzeichen, Mustern oder Modellen, Plänen, geheimen Formeln oder Verfahren oder für die Benutzung oder das Recht auf Benutzung gewerblicher, kaufmännischer oder wissenschaftlicher Ausrüstungen oder für die Mitteilung gewerblicher, kaufmännischer oder wissenschaftlicher Erfahrungen gezahlt werden.

(3) Absatz 1 ist nicht anzuwenden, wenn der in einem Vertragstaat ansässige Empfänger der Lizenzgebühren in dem anderen Vertragstaat, aus dem die Lizenzgebühren stammen, eine Betriebstätte hat und die Rechte oder Vermögenswerte, für die die Lizensgebühren gezahlt werden, tatsächlich zu dieser Betriebstätte gehören. In diesem Fall ist Artikel 7 anzuwenden.

(4) Lizenzgebühren gelten dann als aus einem Vertragstaat stammend, wenn der Schuldner dieser Staat selbst, eines seiner Länder, eine ihrer Gebietskörperschaften oder eine in diesem Staat ansässige Person ist. Hat der Schuldner der Lizenzgebühren, ohne Rücksicht darauf, ob er in einem Vertragstaat ansässig ist oder nicht, in einem Vertragstaat eine Betriebstätte und gehören die Rechte oder Vermögenswerte, für die die Lizenzgebühren gezahlt werden, tatsächlich zu dieser Betriebstätte und trägt die Betriebstätte die Lizenzgebühren, so gelten die Lizenzgebühren als aus dem Vertragstaat stammend, in dem die Betriebstätte liegt.

(5) Bestehen zwischen Schuldner und Gläubiger oder zwischen jedem von ihnen und einem Dritten besondere Beziehungen und übersteigen deshalb die gezahlten Lizenzgebühren, gemessen an der zugrundeliegenden Leistung, den Betrag, den Schuldner und Gläubiger ohne diese Beziehung vereinbart hätten, so wird dieser Artikel nur auf diesen letzten Betrag angewendet. In diesem Fall kann der übersteigende Betrag nach dem Recht jedes Vertragstaates und unter Berücksichtigung der anderen Bestimmungen dieses Abkommens besteuert werden.

Artikel 13

(1) Gewinne aus der Veräußerung unbeweglichen Vermögens im Sinne des Artikels 6 Absatz 2 können in dem Vertragstaat besteuert werden, in dem dieses Vermögen liegt.

(2) Gewinne aus der Veräußerung beweglichen Vermögens, das Betriebsvermögen einer Betriebstätte darstellt, die ein Unternehmen eines Vertragstaates in dem anderen Vertragstaat hat, einschließlich derartiger Gewinne, die bei der Veräußerung einer solchen Betriebstätte (allein oder zusammen mit dem übrigen Unternehmen) erzielt werden, können in dem Staat besteuert werden, in dem die Betriebstätte liegt. Jedoch können Gewinne aus der Veräußerung des in Artikel 19 Absatz 3 genannten beweglichen Vermögens nur in dem Vertragstaat besteuert werden, in dem dieses bewegliche Vermögen nach dem angeführten Artikel besteuert werden kann.

Artikel 14

(1) Vorbehaltlich des Artikels 15 können Vergütungen, die eine in einem Vertragstaat ansässige natürliche Person für unselbständige oder selbständige Arbeit (einschließlich einer freiberuflichen Tätigkeit) bezieht, nur in diesem Staat besteuert werden, es sei denn, daß die Tätigkeit in dem anderen Vertragstaat ausgeübt wird. Wird die Tätigkeit dort ausgeübt, so können diese Vergütungen in dem anderen Staat besteuert werden, jedoch nur inso-

weit, als sie auf die dort ausgeübte Tätigkeit entfallen.

(2) Ungeachtet des Absatzes 1 können Vergütungen, die eine in einem Vertragstaat ansässige natürliche Person für die in dem anderen Vertragstaat ausgeübte Tätigkeit bezieht, nur in dem erstgenannten Staat besteuert werden, wenn

a) der Empfänger sich in dem anderen Staat insgesamt nicht länger als 183 Tage während des betreffenden Steuerjahres aufhält;

b) die Vergütungen von einer Person oder für eine Person gezahlt werden, die nicht in dem anderen Staat ansässig ist, und

c) die Vergütungen nicht von einer Betriebstätte getragen werden, welche die Person, die die Vergütungen zahlt, in dem anderen Staat hat.

(3) Absatz 2 findet keine Anwendung auf Vergütungen, die berufsmäßige Künstler wie Bühnen-, Rundfunk- oder Fernsehkünstler und Musiker sowie Sportler aus ihrer in dieser Eigenschaft persönlich ausgeübten Tätigkeit beziehen.

(4) Ungeachtet der Absätze 1 bis 3 können Vergütungen für unselbständige Arbeit, die an Bord eines Seeschiffes oder Luftfahrzeuges im internationalen Verkehr ausgeübt wird, in dem Vertragstaat besteuert werden, in dem sich der Ort der tatsächlichen Geschäftsleitung des Unternehmens befindet.

Artikel 15

Aufsichtsrats- oder Verwaltungsratsvergütungen und ähnliche Zahlungen, die eine in einem Vertragstaat ansässige Person in ihrer Eigenschaft als Mitglied des Aufsichts- oder Verwaltungsrats einer Gesellschaft bezieht, die in dem anderen Vertragstaat ansässig ist, können in dem letztgenannten Staat besteuert werden.

Artikel 16

(1) Ungeachtet des Artikels 14 können Vergütungen, die die Bundesrepublik, eines ihrer Länder oder eine ihrer Gebietskörperschaften an eine natürliche Person für die der Bundesrepublik, einem ihrer Länder oder einer ihrer Gebietskörperschaften erbrachten Dienste zahlt, nur dann in der Bundesrepublik besteuert werden, wenn der Empfänger Deutscher im Sinne des Artikels 116 Absatz 1 des Grundgesetzes für die Bundesrepublik Deutschland ist.

(2) Ungeachtet des Artikels 14 können Vergütungen, die Argentinien, eine seiner Provinzen oder eine seiner Gebietskörperschaften an eine natürliche Person für die Argentinien, einer seiner Provinzen oder einer ihrer Gebietskörperschaften erbrachten Dienste zahlt, nur dann in Argentinien besteuert werden, wenn der Empfänger argentinischer Staatsbürger ist.

(3) Auf Vergütungen für Dienstleistungen, die im Zusammenhang mit einer kaufmännischen oder gewerblichen Tätigkeit eines Vertragstaates, eines seiner Länder, einer seiner Provinzen oder einer ihrer Gebietskörperschaften erbracht werden, finden die Absätze 1 und 2 keine Anwendung.

Artikel 17

(1) Ruhegehälter und ähnliche Vergütungen, die die Bundesrepublik, eines ihrer Länder oder eine ihrer Gebietskörperschaften zahlt, können nur in der Bundesrepublik besteuert werden.

(2) Ruhegehälter und ähnliche Vergütungen, die Argentinien, eine seiner Provinzen oder eine ihrer Gebietskörperschaften zahlt, können nur in Argentinien besteuert werden.

(3) Ruhegehälter, Renten und andere wiederkehrende oder einmalige Zahlungen, die ein Vertragstaat, eines seiner Länder oder eine ihrer Gebietskörperschaften einer natürlichen Person als Ausgleich für einen Schaden leistet, der als Folge von Kriegshandlungen oder politischer Verfolgung entstanden ist, sind von der Steuer des anderen Vertragstaates befreit.

Artikel 18

Erhält ein Student oder Lehrling, der sich in einem Vertragstaat ausschließlich zum Studium oder zur Ausbildung aufhält und der in dem anderen Vertragstaat ansässig ist oder unmittelbar vorher dort ansässig war, Zahlungen für seinen Unterhalt, sein Studium oder seine Ausbildung, so sind diese Zahlungen von der Steuer des erstgenannten Vertragstaates befreit, sofern sie ihm von außerhalb dieses erstgenannten Vertragstaates zufließen.

Artikel 19

(1) Unbewegliches Vermögen im Sinne des Artikels 6 Absatz 2 kann in dem Vertragstaat besteuert werden, in dem dieses Vermögen liegt.

(2) Bewegliches Vermögen, das Betriebsvermögen einer Betriebstätte eines Unternehmens darstellt, kann in dem Vertragstaat besteuert werden, in dem sich die Betriebstätte befindet.

(3) Seeschiffe und Luftfahrzeuge im internationalen Verkehr sowie bewegliches Vermögen, das dem Betrieb dieser Schiffe und Luftfahrzeuge dient, können nur in dem Vertragstaat besteuert werden, in dem sich der Ort der tatsächlichen Geschäftsleitung des Unternehmens befindet.

Artikel 20

(1) Bei einer in der Bundesrepublik ansässigen Person wird die Steuer wie folgt festgesetzt:

a) Soweit nicht Buchstabe b anzuwenden ist, werden von der Bemessungsgrundlage der deutschen Steuer die Einkünfte aus Quellen innerhalb Argentiniens sowie die in Argentinien gelegenen Vermögenswerte ausgenommen, mit denen sich die vorhergehenden Artikel befassen und die nach diesen Artikeln in Argentinien besteuert werden können. Die Bundesrepublik behält aber das Recht, die auf diese Weise ausgenommenen Einkünfte und Vermögenswerte bei der Festsetzung des Steuersatzes zu berücksichtigen. Auf Dividenden ist Satz 1 nur anzuwenden, wenn sie einer in der Bundesrepublik ansässigen Kapitalgesellschaft von einer in Argentinien ansässigen Kapitalgesellschaft gezahlt werden, deren stimmberechtigte Anteile zu mindestens 25 vom Hundert der erstgenannten Gesellschaft gehören. Von der Bemessungsgrundlage der deutschen Steuer werden ebenfalls Beteiligungen ausgenommen, deren Dividenden nach dem vorhergehenden Satz von der Steuerbemessungsgrundlage ausgenommen sind oder bei Zahlung auszunehmen wären.

b) Auf die deutsche Steuer vom Einkommen, die von den nachstehenden Einkünften erhoben wird, werden angerechnet:

1. bei Dividenden im Sinne des Artikels 10 Absatz 3, mit denen sich Buchstabe a nicht befaßt, ein Betrag in Höhe von 15 vom Hundert des zugeflossenen Dividendenbetrages;
2. bei Zinsen im Sinne des Artikels 11 Absatz 3 ein Betrag in Höhe von 35 vom Hundert des Bruttobetrages der

Zinsen. Wird jedoch der nach argentinischem Recht für Zinsen allgemein geltende argentinische Steuersatz auf einen Satz von weniger als 35 vom Hundert gesenkt, so verringert sich der Anrechnungsbetrag auf den dann zu entrichtenden Betrag der argentinischen Steuer;

3. bei Lizensgebühren im Sinne des Artikels 12 Absatz 2 die für diese Lizenzgebühren entrichtete argentinische Steuer. Ist jedoch die auf diese Lizenzgebühren entfallende argentinische Steuer für eine begrenzte Zeit ganz erlassen oder ermäßigt worden, so wird der Steuerbetrag angerechnet, der nach diesem Abkommen für die Lizenzgebühren hätte entrichtet werden müssen, wenn die Steuer nicht ganz erlassen oder ermäßigt worden wäre;
4. bei den in Artikel 15 angeführten Einkünften die dafür entrichtete argentinische Steuer.

(2) Einkünfte aus Quellen innerhalb der Bundesrepublik sowie in der Bundesrepublik gelegene Vermögenswerte, die nach diesem Abkommen in der Bundesrepublik besteuert werden können, sind von der argentinischen Steuer befreit.

Artikel 21

(1) Die Staatsangehörigen eines Vertragstaates dürfen in dem anderen Vertragstaat weder einer Besteuerung noch einer damit zusammenhängenden Verpflichtung unterworfen werden, die anders oder belastender sind als die Besteuerung und die damit zusammenhängenden Verpflichtungen, denen die Staatsangehörigen des anderen Staates unter gleichen Verhältnissen unterworfen sind oder unterworfen werden können.

(2) Der Ausdruck „Staatsangehörige" bedeutet:

1. in bezug auf die Bundesrepublik alle Deutschen im Sinne des Artikels 116 Absatz 1 des Grundgesetzes für die Bundesrepublik Deutschland sowie alle juristischen Personen, Personengesellschaften und Personenvereinigungen, die nach dem in der Bundesrepublik geltenden Recht errichtet worden sind;
2. in bezug auf Argentinien alle argentinischen Staatsbürger sowie alle juristischen Personen, Personengesellschaften und Personenvereinigungen, die nach dem in Argentinien geltenden Recht errichtet worden sind.

(3) Die Besteuerung einer Betriebstätte, die ein Unternehmen eines Vertragstaates in dem anderen Vertragstaat hat, darf in dem anderen Staat nicht ungünstiger sein als die Besteuerung von Unternehmen des anderen Staates, die die gleiche Tätigkeit ausüben.

Diese Bestimmung ist nicht so auszulegen, als verpflichte sie einen Vertragstaat, den in dem anderen Vertragstaat ansässigen Personen Steuerfreibeträge, -vergünstigungen und -ermäßigungen auf Grund des Personenstandes oder der Familienlasten zu gewähren, die er den in seinem Hoheitsgebiet ansässigen Personen gewährt.

(4) Die Unternehmen eines Vertragstaates, deren Kapital ganz oder teilweise, unmittelbar oder mittelbar, einer in dem anderen Vertragstaat ansässigen Person oder mehreren solchen Personen gehört oder ihrer Kontrolle unterliegt, dürfen in dem erstgenannten Vertragstaat weder einer Besteuerung noch einer damit zusammenhängenden Verpflichtung unterworfen werden, die anders oder belastender sind als die Besteuerung und die damit zusammenhängenden Verpflichtungen, de-

nen andere ähnliche Unternehmen des erstgenannten Staates unterworfen sind oder unterworfen werden können.

(5) In diesem Artikel bedeutet der Ausdruck „Besteuerung" Steuern jeder Art und Bezeichnung.

Artikel 22

(1) Ist eine in einem Vertragstaat ansässige Person der Auffassung, daß die Maßnahmen eines Vertragstaates oder beider Vertragstaaten für sie zu einer Besteuerung geführt haben oder führen werden, die diesem Abkommen nicht entspricht, so kann sie unbeschadet der nach innerstaatlichem Recht dieser Staaten vorgesehenen Rechtmittel ihren Fall der zuständigen Behörde des Vertragstaates unterbreiten, in dem sie ansässig ist.

(2) Hält diese zuständige Behörde die Einwendung für begründet und ist sie selbst nicht in der Lage, eine befriedigende Lösung herbeizuführen, so wird sie sich bemühen, den Fall durch Verständigung mit der zuständigen Behörde des anderen Vertragstaates so zu regeln, daß eine dem Abkommen nicht entsprechende Besteuerung vermieden wird.

(3) Die zuständigen Behörden der Vertragstaaten werden sich bemühen, Schwierigkeiten oder Zweifel, die bei der Auslegung oder Anwendung des Abkommens entstehen, in gegenseitigem Einvernehmen zu beseitigen. Sie können auch gemeinsam darüber beraten, wie eine Doppelbesteuerung in Fällen, die in dem Abkommen nicht behandelt sind, vermieden werden kann.

(4) Die zuständigen Behörden der Vertragstaaten können zur Herbeiführung einer Einigung im Sinne der vorstehenden Absätze und zum Zwecke des in Artikel 23 vorgesehenen Austausches von Informationen unmittelbar miteinander verkehren.

Artikel 23

(1) Die zuständigen Behörden der Vertragstaaten werden die Informationen austauschen, die zur Durchführung dieses Abkommens erforderlich sind. Alle so ausgetauschten Informationen sind geheimzuhalten und dürfen nur solchen Personen oder Behörden zugänglich gemacht werden, die mit der Veranlagung oder Erhebung der unter das Abkommen fallenden Steuern befaßt sind.

(2) Absatz 1 ist auf keinen Fall so auszulegen, als verpflichte er einen der Vertragstaaten:

a) Verwaltungsmaßnahmen durchzuführen, die von den Gesetzen oder der Verwaltungspraxis dieses oder des anderen Vertragstaates abweichen;

b) Angaben zu übermitteln, die nach den Gesetzen oder im üblichen Verwaltungsverfahren dieses oder des anderen Vertragstaates nicht beschafft werden können;

c) Informationen zu erteilen, die ein Handels-, Geschäfts-, Gewerbe- oder Berufsgeheimnis oder ein Geschäftsverfahren preisgeben würden oder deren Erteilung der öffentlichen Ordnung widerspräche.

Artikel 24

Dieses Abkommen berührt nicht die steuerlichen Vorrechte, die den diplomatischen und konsularischen Bediensteten nach den allgemeinen Regeln des Völkerrechts oder auf Grund besonderer Vereinbarungen zustehen.

Artikel 25

Enthalten das Recht eines der beiden Vertragstaaten oder völkerrechtliche Regelungen, die zwischen den Vertragstaaten neben diesem Abkommen gegenwärtig oder künftig bestehen, eine Bestimmung,

die für eine in einem Vertragstaat ansässige Person günstiger ist als Regelungen dieses Abkommens, so wird diese Bestimmung, soweit sie günstiger ist, von diesem Abkommen nicht berührt.

Artikel 26

Dieses Abkommen gilt auch für das Land Berlin, sofern nicht die Regierung der Bundesrepublik Deutschland gegenüber der Regierung der Argentinischen Republik innerhalb von drei Monaten nach Inkrafttreten des Abkommens eine gegenteilige Erklärung abgibt.

Artikel 27

(1) Dieses Abkommen bedarf der Ratifikation; die Ratifikationsurkunden sollen so bald wie möglich in Bonn ausgetauscht werden.

(2) Dieses Abkommen tritt einen Monat nach Austausch der Ratifikationsurkunden in Kraft und gilt dann für die Steuern, die für das dem Jahr des Austauschs der Ratifikationsurkunden folgende Kalenderjahr, sowie für die darauf folgenden Kalenderjahre erhoben werden.

(3) Ungeachtet des Absatzes 2 gilt Artikel 8 für die Steuern, die für das Kalenderjahr 1961 und für die darauf folgenden Kalenderjahre erhoben werden.

Artikel 28

(1) Dieses Abkommen bleibt auf unbegrenzte Zeit in Kraft, jedoch kann nach Ablauf von fünf Jahren seit seinem Inkrafttreten jeder Vertragstaat bis einschließlich dreißigsten Juni jeden Kalenderjahres das Abkommen gegenüber dem anderen Vertragstaat auf diplomatischem Wege schriftlich kündigen; in diesem Fall ist das Abkommen erstmals nicht mehr anzuwenden auf die Steuern, die für das auf das Kündigungsjahr folgende Kalenderjahr erhoben werden.

(2) Artikel 11 und Artikel 20 Absatz 1 Buchstabe b Nummer 2 sind nicht mehr anzuwenden auf Zinsen, die am oder nach dem ersten Januar gezahlt werden, der dem Jahr folgt, in dem die Kündigung erstmals ausgesprochen werden könnte.

GESCHEHEN zu Buenos Aires am dreizehnten Juli neunzehnhundertsechsundsechzig in vier Urschriften, je zwei in deutscher und in spanischer Sprache, wobei jeder Wortlaut gleichermaßen verbindlich ist.

Für die Bundesrepublik Deutschland
Dr. Karl Carstens
Staatssekretär des Auswärtigen Amtes

Für die Argentinische Republik
Dr. Nicanor Costa Mendez
Minister für Auswärtige Beziehungen und Kultus

Notenwechsel

Der Staatssekretär
des Auswärtigen Amtes

Buenos Aires, den 13. Juli 1966

Exzellenz,

anläßlich der heutigen Unterzeichnung des Abkommens zwischen der Bundesrepublik Deutschland und der Argentinischen Republik zur Vermeidung der Doppelbesteuerung auf dem Gebiete der Steuern vom Einkommen und vom Vermögen beehre ich mich, Ihnen im Namen der Regierung der Bundesrepublik Deutschland mitzuteilen, daß die beiden

Vertragstaaten vereinbart haben, daß die nachstehend aufgeführten Vorschriften wie folgt anzuwenden sind:

Artikel 20 Absatz 1 Buchstabe a gilt für eine Betriebstätte oder für die von einer Gesellschaft ausgeschütteten Dividenden nur dann, wenn die Gewinne der Betriebstätte oder die Einkünfte der Gesellschaft ausschließlich oder fast ausschließlich stammen:

a) aus einer der folgenden innerhalb Argentiniens ausgeübten Tätigkeiten, nämlich aus der Herstellung oder dem Verkauf von Gütern oder Waren, aus Vermietung oder Verpachtung, aus Dienstleistungen oder aus Bank- oder Versicherungsgeschäften; oder

b) aus Dividenden, die von einer oder mehreren in Argentinien ansässigen Gesellschaften gezahlt werden, deren stimmberechtigte Anteile zu mehr als 25 vom Hundert der erstgenannten Gesellschaft gehören und die ihre Einkünfte wiederum ausschließlich oder fast ausschließlich aus einer der folgenden innerhalb Argentiniens ausgeübten Tätigkeiten beziehen, nämlich der Herstellung oder dem Verkauf von Gütern oder Waren, aus Vermietung oder Verpachtung, aus Dienstleistungen oder aus Bank- oder Versicherungsgeschäften.

Sind diese Voraussetzungen nicht erfüllt, so wird die für die Betriebstätte oder die Dividenden gezahlte argentinische Steuer auf die dafür zu zahlende deutsche Steuer angerechnet.

Ich wäre dankbar, wenn Sie mir Ihr Einverständnis mit dem Vorstehenden bestätigten; in diesem Fall sollen die vorliegende Note und Ihre Antwortnote als Bestandteil des Abkommens gelten.

Carstens

Seiner Exzellenz
Herrn Dr. Nicanor Costa Mendez
Minister für Auswärtige Beziehungen und Kultus
Buenos Aires

(Übersetzung)

Poder Ejecutivo Nacional
Ministerio de Relaciones Exteriores y Culto

Buenos Aires, den 13. Juli 1966

Exzellenz,

Ich beehre mich, Euerer Exzellenz im Namen der Regierung der Argentinischen Republik mein Einverständnis mit dem vorstehenden Text*) zu bestätigen; Ihre Note und diese Antwortnote sollen als Bestandteile des Abkommens gelten.

Ich begrüße Euere Exzellenz mit ausgezeichneter Hochachtung.

Dr. Nicanor Costa Mendez

Seiner Exzellenz Herrn Dr. Karl Carstens
Staatssekretär im Auswärtigen Amt der
Bundesrepublik Deutschland

Buenos Aires

*) Für Note vom 13. Juli 1966, siehe S. B14.

Supplement **C**

First Independence Budget of Guyana

SUPPLEMENT TO THE BULLETIN FOR INTERNATIONAL FISCAL DOCUMENTATION
AU BULLETIN DE DOCUMENTATION FISCALE INTERNATIONALE

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INTERNATIONAL BUREAU OF FISCAL DOCUMENTATION

Muiderpoort – 124 Sarphatistraat – Amsterdam

INTRODUCTION

Sessional Paper No. 1/67 of the First House of Assembly under the Constitution of Guyana contains the Budget Speech by The Hon. Peter S. d'Aguiar, M.P., held on the 16th January 1967. It is the first budget since Guyana achieved independent status.

One of the big problems of developing countries is the fiscal and financial organisation: how to collect taxes efficiently and to improve the methods for catching tax dodgers, how to spend public funds economically and in the amounts and for the purposes for which they were provided.

As the Minister stated in his budget speech, tax collection is most hindered by the shortage of a professional skilled staff. Financial control is inadequate due to the inefficiency of the accounting system. The fiscal and financial organisation is not good and must be improved! Similar views were expressed during the advanced seminar in Current Problems and Training Needs in Tax Administrations, held at Addis Ababa in December 1965 in which the Seminar Heads of Taxation Departments in Africa exchanged views.

The aid of mechanical or electronic systems in the tax administrations may be very useful. During the African Seminar it was felt that greater speed and precision could be achieved by mechanisation although labour costs could not be reduced. The African states, which have introduced such a system, e.g. Nigeria, Ghana, Ivory Coast, Madegascar, Cameroun and U.A.R. warned of mistakes, made by tax officials not fully aware of the inherent requirements and workings of the machines; implying a warning to those countries considering the introduction of mechanisation to start from the beginning with a unified system.

In Guyana no mechanical aid has been used for the tax collection so far although recently an electro-mechanical accounting system has been introduced which can provide prompt information on the expenditure of public funds.

The effectiveness of this system, which may be a considerable help in ensuring that public funds are spent economically, depends—as is implied in the Minister's speech—'on the sense of responsibility, which all those whose duty it is to expend public moneys show in their work'.

We think that, whether it is spending public funds or collecting taxes, this human facet is the most important one. Even with the best material, the highway to prosperity cannot be constructed without a high degree of sense of responsibility among its constructors.

Budget speech

by

The Hon. Peter S. d'Aguiar, M. P.
Minister of Finance

16th January, 1967.

The budget I now present to this Honourable Assembly proposes expenditure of nearly $ 129 mn. on current and capital services. It is the first independence budget. It reflects the full costs of running the government of a sovereign nation. We are now masters of our own destiny. We must rely on ourselves to improve our lot. We have a good country with many natural advantages. We have many friends who have generously demonstrated their willingness to help us. But it is only by helping ourselves that we can put this generous assistance to good use and achieve a better life. This involves some sacrifice, but nothing worthwhile can be achieved painlessly.

We have made good progress in the past two years. Peace and confidence in the future have been restored. Capital inflow from abroad, which is a measure of the confidence the outside world places in our future, has expanded from about $ 15 mn. in 1964 to $ 30 mn. in 1966. This year it should rise to about $ 50 mn. With the help of these funds from abroad and our own savings, gross domestic investment—total investment in the country—has risen from about $ 55 mn. in 1964 to nearly $ 100 mn. in 1966. In the past two years the Government has raised $ 21½ mn. from voluntary subscriptions to its issues of Treasury Savings Certificates and debentures—more than was raised in the previous quarter of a century and about four times as much as was raised by forced subscriptions in 1962 and 1963. The response of the revenue has been remarkable. It has grown by $ 16 mn. (25%) in the last two years, of which by far the greater part ($ 13½ mn.) was due to the buoyancy of the economy; $ 2½ mn. came from higher taxation. The Government's revenue—the ordinary revenues from taxes, fees, property and enterprise—has grown just as fast as the national income.

But we have been trying, especially in the past year, to take more out of the economy than we have put in. We are tending to live above our means. Demands for a standard of living higher than the country can afford at present can gain us nothing but can frustrate our efforts to develop the economy and realise our aspirations for a better life. Interruptions of production arising from wage demands which can not be supported at the present level of productivity will defeat the whole scheme of development by wasting productive capacity and discouraging the investment without which there can be no prosperity.

The expenditure of $ 129 mn. the budget calls for is $ 13 mn. more than we spent last year, and nearly $ 50 mn. more than we spent in 1964. The greater part of the increase—nearly $ 30 mn.—since 1964 is for development works and services. A further $ 4 mn. of the increase goes indirectly into development by way of the additional debt charges incurred since 1964 to support the borrowing for development. Fortunately, we have been able to borrow on better terms

recently thus lightening the burden of these debt charges. The costs of independence have added something like $ 6 mn. to our expenditure.

The money that Government spends is coming out of the pockets of all of us. We must see that it is spent effectively and economically for its purposes so that we as a community get full value for our money. This is the purpose of good government.

RESULTS AND PROSPECTS

Production (as measured by the gross domestic product at factor cost) in Guyana in 1966 totalled about $ 360 mn.—$ 60 mn. or 20% more than in 1964. Thus, in spite of lower average export prices for sugar and rice, which account for a fifth of the product, the country's production has been rising since 1964 at the rate of about 10% per annum in value. With the tumble in world sugar prices, exports fell from a peak level of $ 175 mn. in 1963 to $ 167 mn. in 1965. But in 1966 they reached their highest level ($ 180 mn.) in spite of the continuing low level of sugar prices. This success is attributable to the bauxite-alumina industry. With the assurance given by this Government when it assumed office of a stable basis for development, the industry has increased its annual production by $ 20 mn. (30%) since 1964. The full fruits of the development thus initiated will not be garnered until after 1967, when, with the development of additional calcining capacity, production should rise by a further $ 10 mn. per annum.

This higher level of production has raised local incomes (the gross national income and product at factor cost) by some $ 60 mn.—22%—since 1964. National income per head of population rose from $ 400 in 1964 to $ 470 in 1966—an increase of 18%.

But local expenditure (domestic expenditure on goods and services at factor cost) on public and private consumption and investment has expanded even more—by about $ 100 mn. (a third) since 1964. The gap of $ 40 mn. between income and expenditure was covered mainly by gifts, loans, and direct investment (capital inflow) from abroad but partly by running down our reserves of foreign exchange (the nation's bank balance). Both in 1965 and 1966 the nation had to run down its reserves of foreign exchange in order to finance the heavy demand for imports.

Looked at from another viewpoint, the increase in our annual consumption and investment ($ 100 mn.) since 1964 could not be supplied entirely from the increase in our own resources (the increased production of $ 60 mn.). We had to make good the deficiency by expanding our imports (of which commodity imports rose by $ 50 mn. to an all-time record in 1966 of $ 200 mn.) beyond the level we could finance from exports and capital inflow.

We have been spending heavily on development. Gross investment (nearly $ 100 mn. or 22% of total expenditure in 1966) was $ 40 mn. or 75% higher than in 1964, of which the increase in Government investment accounted for about half. Foreign-owned companies invested $ 35 mn. in 1966 as compared with $ 25 mn. in 1965 and $ 20 mn. in 1964. Private building and construction, which by 1964 had fallen from the high level of $ 14 mn. in 1960 to $ 7 mn. in 1964, had expanded by 1966 to $ 15 mn. Government building and construction in 1966 was some $ 12 mn. higher than in 1964.

This is a picture of an economy which, despite the setbacks of low world prices for its principal agricultural crops, sugar and rice, has nevertheless stirred itself from the

doldrums of 1963 and 1964 and by dint of hard pushing by the Government (which has expanded its expenditure, mainly on the economic, social and administrative development required for an independent Guyana, by $ 35 mn. or nearly 50% since 1964), and the resurgence of confidence and private investment, is forcing the pace of its development with the inevitable strains and stresses.

But since the slack in the economy at the beginning of this effort has now been fully taken up, we can only maintain this increasing tempo of development by holding down expenditure on consumption, especially on non-essential imports. We can not take out of the economy more by consumption and investment than we put in by production or can entice from abroad. We can consume more only if we produce more; we can earn more only if we produce more. To think otherwise is to delude ourselves. To absorb our unemployment and to raise the community's standard of living we must invest heavily. If this objective is to be achieved, consumption must be restrained and must be directed in such a way that local production benefits. The country must increase its production to expand employment and reduce the level of its imports. When we spend we must think not only of what we can get for our money but also how much we can increase our earnings by buying local products in preference to imports. Keep the money at home where it can multiply and fructify.

If we can moderate our propensity to import, the outlook for next year is good. There should be a moderate rise of perhaps as much as $ 10 mn. in exports. The inflow of capital from abroad to help us in our development effort could be as much as $ 20 mn. higher than in 1966. It should therefore be possible to redress any imbalance in our international payments. But all will be lost if we as workers or consumers try to get more out of the economy than we are putting in. The mission from the International Monetary Fund which recently examined our economy in its fiscal and monetary aspects was satisfied that it was in good health in spite of the strains and stresses to which I have referred. We must keep it so.

1966 REVENUE AND CURRENT EXPENDITURE

The 1966 Estimates provided for current expenditure of $ 84.2 mn. It was estimated that the revenue, including a special budgetary grant from the United Kingdom Government of $ 4.8 mn., would just about cover this expenditure. The 1966 Revised Estimates indicate a surplus of $ 0.8 mn., including only $ 3 mn. of the United Kingdom budgetary grant. Indeed, since the revised estimate of the surplus is based on a re-definition of the ordinary revenues to exclude capital receipts of $ 0.6 mn. formerly treated as current receipts, the result for the year is likely to be $ 1.4 mn. better than the forecast, despite the fact that United Kingdom support was $ 1.8 mn. less than estimated.

The actual yield of the revenue ($ 86.3 mn. per the Revised Estimates) was $ 2.7 mn. more than estimated. Indeed, if the United Kingdom grant is excluded, the actual yield ($ 83.3 mn.) was $ 4.5 mn. (nearly 6%) higher than the projected yield ($ 78.8 mn.) and 6 mn. (8%) higher than actual receipts in 1965. At $ 32.5 mn. import duties yielded $ 1.3 mn. less than the estimate ($ 33.8 mn.) and $ 4.5 mn. more than the actual receipts in 1965. $ 2.5 mn. of this increase over the 1965 yield must be attributed to the increased rates of duty introduced with the last

budget; the remaining $ 2 mn. (7%) reflects the growth in the value of imports. The yield ($ 9.5 mn.) of excise duties was higher than expectations ($ 9.2 mn.) and $ 1.1 mn., or nearly 15%, higher than in the previous year. The other major element of the revenue—income tax—yielded $ 25 mn., about the same as in the previous year, and $ 4.5 mn. higher than expectations when the budget was framed. The other significant deviations from the Approved Estimates relate to the United Kingdom grant and Currency Board profits, which together show a net reduction of $ 1.0 mm. Both are subject to adjustment.

The revenue has been remarkably buoyant since 1965. Between 1961 and 1964 it had risen by only about $ 8 mn. (13%), the bulk of which was attributable to higher rates of taxation. Between 1964 and 1966 the revenue (excluding the United Kingdom budgetary grant) rose by $ 16 mn. (25%), of which only $ 2.5 mn. was attributable to higher rates of taxation. Between 1964 and 1966 the G.D.P. at factor cost rose by 20%; the revenue (excluding the yield of higher taxation introduced in 1966 and the United Kingdom budgetary grant) rose by the same percentage. The revenue is thus fully responsive to changes in the national income.

Current expenditure in 1966 is now estimated at $ 85.4 mn.—only $ 1.2 mn. more than the Approved Estimates despite supplementary provision of $ 6.3 mn. Thus, the greater part of the supplementary provision was offset by savings elsewhere. The actual expenditure in 1965 was $ 82. mn., so that expenditure in 1966 ($ 85.4 mn.) was $ 3.4 mn. higher than in the previous year. The significant increases on 1965 expenditure were: under Public Debt—$ 1.1 mn.; under Refunds of Revenue—$ 1.3 mn.; under Defence—$ 1.1 mn.; under Police and Prisons—$ 0.6 mn.; under Agriculture—$ 0.6 mn.; and under External Affairs—$ 0.3 mn. There were substantial reductions under Special Service Unit and General Emergency totalling $ 0.8 mn.; under Transport and Harbours—$ 0.8 mn.; under Works and Hydraulics—$ 0.4 mn.; and under Revision of Wages, etc.—$ 0.6 mn.

1967 CURRENT EXPENDITURE

The Estimates of Current Expenditure now presented to this Assembly call for expenditure of $ 89.4 mn.—$ 4 mn. higher than the Revised Estimates for 1966 and $ 7.4 mn. higher than the actual expenditure in 1965. Public debt charges account for $ 1.5 mn. of the increase of $ 4.0 mn. on 1966 expenditure. Debt charges have grown from nearly $ 6 mn. (12% of expenditure) in 1960 to $ 14.5 mn. (16% of expenditure) in 1967. This growth reflects the consequences of a development programme involving expenditure of about $ 170 mn. during the period. For this, the Government will have borrowed about $ 50 mn. in each of the periods 1960 to 1964 and 1965 to 1967. Fortunately, we have been able to get better terms recently. The USAID loans are for a period of 40 years with a moratorium of 10 years, and carry interest at 1% per annum during the moratorium and thereafter at 2½% per annum. The latest United Kingdom loans, which are repayable over 25 years, allow a waiver of interest for 6 years and a 2-year grace period for repayment followed by 5 years of graduated payments. A 50-year interest-free loan with a 10-year moratorium has been granted by Canada for topographical surveys. Moreover, we have been able to avoid contractor-finance

arrangements, the high cost and short currency of which throw a heavy burden of debt charges on the budget.

The remainder of the increase arises from Personal Emoluments—for new posts, the filling of vacant posts and salary increments. The increases fall mainly under Defence ($ 0.8 mn.), Police and Prisons ($ 0.5 mn.), External Affairs ($ 0.5 mn.), Works and Hydraulics ($ 0.4 mn.), Education ($ 1.1 mn.), and Health ($ 0.7 mn.); with an offsetting reduction ($ 0.6 mn.) for the Telecommunications Department which will be established as a separate corporation very shortly. Personal Emoluments now account for 44% of the expenditure under the Current Estimates as compared with 41% in Trinidad. Our high percentage (44%), though not the highest, is among the highest in the world and must cause us some concern.

The Other Charges provision has been reduced by $ 1.3 mn. under General Emergency, by $ 0.2 mn. included last year for the ex gratia payment to Government workers in respect of pay lost during the 1963 strike, and by removal from the Estimates of provision ($ 0.5 mn.) for the Telecommunications Department.

I referred last year to the mountain of subsidies largely hidden in the public debt charges which required for their accommodation a large proportion (a fifth) of the Government's revenues. The major group, as I pointed out, comprised the subsidies that go into agriculture mainly through the unrecouped capital charges on drainage and irrigation and land development works and guaranteed prices for farm produce. The Government proposes in 1967 to formulate detailed proposals for a substantial reduction and rationalisation of these subsidies so as to relieve the public purse of some of this burden and to provide incentives in new directions necessary for the development of local crops to replace imports.

Current expenditure has expanded from $ 70 mn. in 1964 to nearly $ 90 mn. projected for 1967—an increase of nearly 30%. Three-fifths of this increase arises from Debt Charges ($ 4 mn.), Education ($ 4½ mn.), Health ($ 2½ mn.) and Agriculture, Forests and Mines ($ 1 mn.). Of the remainder, $ 2½ mn. for Defence, $ 1½ mn. for Police, $ 1 mn. for External Affairs, and perhaps a further $ 1 mn. for expansion of the other administrative services, contributions to international bodies, etc., may be regarded as the direct costs of independence. The remaining $ 2 mn. has been absorbed in price and wage increases of one kind or another.

The Estimates for 1967 have been very tightly framed. Strict control and every effort at economy will be necessary if expenditure is to be kept within their bounds. Past history in this respect has not been satisfactory although there are signs of greater awareness of the need for control and economy.

1967 CURRENT RECEIPTS

The current receipts of the Government—its ordinary revenues—are expected to yield $ 89.1 mn. This is $ 2.8 mn. more than the Revised Estimates for 1966 ($ 86.3 mn.) and $ 11.8 mn. more than the actual receipts in 1965 ($ 77.3 mn.). Since the 1966 current receipts include an extraordinary receipt of $ 3 mn. from the special United Kingdom budgetary grant, the regular elements of the 1967 current receipts are in fact projected at a level $ 5.8 mn. or 7% higher than in 1966.

Import duties are estimated to yield $ 34 mn.—$ 1.5 mn. more than the 1966 revised estimate ($ 32.5 mn.). The estimate allows for a full year's yield at the higher rates of duty introduced last year on a level of imports $ 15 mn. (7½%) higher than this year's, but with a greater proportion of capital goods dutiable at low rates.

It has been assumed that the excise yield will rise by 4% to $ 9.9 mn., which is perhaps optimistic in view of the sharp rise in 1966 due to the special circumstances of that year.

The income tax yield this year is estimated to be $ 27.5 mn.—$ 2.5 mn. or 10% higher than last year's. The incomes of companies and traders in 1966 should provide $ 2 mn. of this increase and PAYE incomes (from employment, etc.) in 1967, the remaining $ 0.5 mn. (5% increase).

The higher rates of vehicle licence duties and the travel tax introduced in the last budget effectively from this year should add about $ 0.5 mn. to the revenue.

Arrears of rent, royalties, interest and Currency Board profits account for about $ 1½ mn. of the estimated increment in revenue this year. With the establishment of a separate corporation to administer telecommunications, the gross revenue (about $ 1¼ mn. per annum) from this source will no longer appear in the Estimates; however, interest charges will include $ 0.6 mn. from the yield of debentures held by the Government against assets handed over to the corporation.

SUMMARY OF CURRENT ESTIMATES

From the foregoing, it is evident that insofar as the Current Budget is concerned results last year and prospects this year give no cause for concern. With $ 3 mn. of the United Kingdom special grant included, the 1966 Current Estimates show a surplus of $ 0.8 mn. On the estimates I have just discussed the 1967 Current Estimates show only a small deficit ($ 0.3 mn.)—a net surplus for the two years of $ 0.5 mn.—and I have hopes that with effective expenditure control, the actual results for 1967 will show a surplus.

However, our development effort requires that the revenue should be made to contribute substantially towards the financing of capital expenditure. This is necessary for three reasons. First, our development needs are so pressing and so huge that even the generous level of assistance made available to us on soft loan or grant is insufficient; and hard loans, both internal and external, are limited in supply and limited by our ability to bear the burden of their heavy loan charges. Secondly, foreign assistance tends to be limited (although fortunately with some exceptions) to the import content of projects and for this and other reasons many worthy schemes have to depend in whole or in part on local funds. Thirdly, to get our friends to help us, we must show them that we are really trying to help ourselves.

1966 CAPITAL ESTIMATES

Capital expenditure last year totalled $ 30.4 mn.—$ 6.3 mn. more than in 1965 and $ 20.8 mn. more than in 1964. Of this expenditure sea defences, drainage and irrigation works, land clearance and other agricultural works and services accounted for $ 6.0 mn.; roads accounted for $ 7.0 mn.; the railways, steamers and airways for $ 1.6

mn.; the Bank of Guyana (building and other capital) for $ 2.3 mn.; school buildings and other capital for education for $1.5 mn.; health for $ 0.7 mn.; housing for $ 0.6 mn.; and defence and police for $ 1.5 mn. $ 2 mn. was spent on loans to corporations and for other development purposes and on contributions to internal and external financial institutions.

This expenditure ($ 30.4 mn.) was financed to the extent of $ 21.5 mn. from revenue, grants and loans received during the year. There was thus a deficiency in cash accounting terms of $ 8.9 mn. However, a further $ 4.2 mn. was receivable at the end of the year against expenditure incurred in 1966, so that the true deficit was $ 4.7 mn.

Of the total of $ 25.7 mn. received or receivable in 1966, local funds supplied $ 8.9 mn. (33%)—$ 8.1 mn. from local issues of debentures and Treasury Savings Certificates and $ 0.8 mn. from revenue receipts of a capital nature or earmarked for capital expenditure. Foreign aid provided $ 16.8 mn. (67%)—$ 11.1 mn. in the form of grants and $ 5.7 mn. in the form of loans.

The response to the Government's efforts to raise local loans is very heartening. In the two years 1965 and 1966, $ 21.5 mn. was raised by the issue of Treasury Savings Certificates and debentures—more than was raised in the past 25 years by voluntary subscriptions, and nearly four times the amount raised by forced subscriptions in 1962 and 1963.

The deficit of $ 8.9 mn. (of which $ 4.2 mn. was covered by anticipated further receipts in 1967 against 1966 expenditure) together with the accumulated capital deficits of previous years ($ 8.2 mn.)—a total of about $ 17 mn.—was financed by bank overdraft and Treasury Bills. This kind of financing has been carried as far as is practicable and desirable. Further deficits on capital account must be avoided.

1967 CAPITAL ESTIMATES

The Capital Estimates as now presented to this Assembly call for expenditure of $ 39.2 mn.—$ 8.8 mn. more than the actual expenditure in 1966. This, I feel, is for the first time in our history a realistic estimate of what capital works and services are feasible of execution in a year and can be financed from the funds likely to be available.

The provision proposed for sea defences is $ 1.5 mn.—for works of the highest priority, certainly well within the capacity of the department to execute; and that for drainage and irrigation and other agricultural works and services, $ 2.1 mn. Roads carry provision totalling $ 9.5 mn., of which the Atkinson Field-Mackenzie road accounts for $ 7 mn. Feasibility surveys for the West Coast and the Corentyne roads are being undertaken with a view to financing their reconstruction from USAID loans. Railways, steamers and airfields (including the new airport building and the rehabilitation of the runways at Atkinson Field) account for $ 3.4 mn. The University of Guyana and the school building programmes should absorb $ 2.5 mn. Surveys—hydro-electric, geological, forest and topographic—of our natural resources call for expenditure of some $ 3.7 mn. Housing and buildingland development require provision of $ 1.1 mn. Loans for various development purposes require provision of $ 4.5 mn. Equipment and vehicles for various purposes call for provision of $ 2.9 mn.

In addition to $ 4.2 mn. receivable in respect of 1966 expenditure, funds in sight for the purposes of 1967 expenditure total $ 34.9 mn.—$ 4.3 mn. from miscellaneous

capital revenues (the major element being the expected distribution by mid-1967 of the surplus assets of the Currency Board); $12.0mn. from foreign grants; $ 15.6 mn. from foreign loans; and $ 3.0 mn. from local loans. Receipts against this year's expenditure are thus $ 4.3 mn. less than the projected expenditure.

SUMMARY OF FINANCIAL POSITION

At the end of 1965 the Government owed the banks $ 5.9 mn., and holders of Treasury Bills $ 1.8 mn.—a total of $ 7.7 mn. With a surplus of $ 0.8 mn. on current account, a deficit on capital account of $ 8.9 mn. and a further advance of $ 1.0 mn. to the Rice Marketing Board, this short-term indebted ness had risen to about $ 17 mn. at the end of 1966. Of this short-term indebtedness of $ 17 mn. at the end of 1966, about $ 15 mn. was supplied by the banking system.

This short-term indebtedness is all attributable to capital account, which was overdrawn by about $ 17 mn. at the end of 1966, and reflects the strain on our finances arising from the high level of development expenditure—$ 55 mn. in two years.

The 1967 budget as presented projects a deficit of $ 0.3 mn. on current account and a deficit of $ 0.1 mn. on capital account (including $ 4.2 mn. receivable in 1967 in respect of 1966 expenditure). Indeed, if only capital receipts against 1967 capital expenditure are taken into account, the total budget in 1967 is in deficit by $ 4.6 mn.

Steps must be taken to remove this deficit and reduce the short-term debt to manageable proportions.

As I have indicated earlier in my speech, the economic and financial situation requires that the current budget should throw up a surplus to help finance capital expenditure and liquidate some of the short-term indebtedness. Fiscal and monetary measures must be taken to relieve the pressure of demand for imports in the short-run and to increase local production for import substitution in the longer run. The Government has had the assistance of missions from both the International Bank for Reconstruction and Development and the International Monetary Fund in formulating a policy that will achieve these results.

The present economic structure and circumstances require that the main assault be levelled at imports. The pressure of demand, which the high level of Government deficit spending on investment has generated, has with the high propensity of the community to import, raised imports to a level beyond the bounds set by the foreign exchange the country can earn from its exports or beg, borrow or entice from abroad. Higher taxation on imports will, in the short-run, help to restrain the demand for imports (by raising their cost and mopping up some of the disposable income of the community now directed to imports) and provide some of the additional revenue required to throw up a budget surplus. In the longer run it will help towards import substitution.

The Government therefore proposes to introduce the following revenue measures, yielding $ 5.4 mn. per annum as follows:—

(i)	Additional import duties	$ 2.55 mn.
(ii)	Higher excise duty on matches	$ 0.05 mn.
(iii)	Higher trade licence duties	$ 0.15 mn.
(iv)	Licence duties on betting shops	$ 0.05 mn.
(v)	Higher duties on transfers of property	$ 0.10 mn.
(vi)	Tax on long-term capital gains at 10%	—

(vii) Spreading initial allowances granted under Income Tax (In Aid of Industry) Ordinance $ 2.5 mn.

The additional import duties will be imposed on a limited range of imports—less than 10% by value of the total. Of these imports, alcoholic drinks and tobaccos will provide about 40% of the additional yield. The price effect of the additional duties on these groups of commodities will be such as to add about 2c to the price of a packet of local cigarettes and $ 1.50 to the price of a bottle of whisky. Guyana certainly produces an adequate quantity and range of alcoholic liquors—and, I am sure, can produce more varieties; and there is no reason why she should not produce more of her tobacco needs. If we must spend scarce foreign exchange on liquor and tobacco and stint our contribution to local employment, we should not grudge a bigger contribution to the revenue. The additional duty on non-essential food stuffs and on clothing should provide 30% of the increased yield. Here again we can buy more local produce with benefit to local employment. The increased rates applicable here are 5% *ad valorem* on commodities now subject to duty at rates not exceeding 20% preferential and 40% general and 10% on commodities now carrying higher rates of duty. The price effect is therefore small. The same scheme of additional duties (5% and 10% *ad valorem*) will apply to consumer durables and miscellaneous manufactured goods, which should provide 30% of the increased yield. I hasten to assure the ladies that I have no designs on their cosmetics. These increased duties will raise the index of retail prices by less than one point.

It is also proposed to make certain adjustments to the tariff of small revenue significance to correct anomalies or as concessions to industry, e.g. the rates of duty on trailers for agricultural use will be dutiable at 5% preferential and 10% general, instead of the present rates 20% and 40% respectively, and the frames of pre-fabricated buildings for industrial use will be dutiable at 5% and 10% instead of 20% and 40%, preferential and general, respectively.

The excise duty on matches will be increased from 25c to 50c per gross boxes raising the controlled price retail from 2½c to 3c a box, but leaving the effective retail price—the price for a single box—at 3c.

The trade licence duties were last revised in 1940 when the rental values on which they were based were less than half the present levels. The upper limit of licence duty in Georgetown and New Amsterdam is now $ 250 per annum for a rental value in excess of $ 10,000 per annum. The effect of the increased rates proposed for Georgetown and New Amsterdam will be to increase the licence duty for rental values up to $ 200 a month by $ 5 to $ 15 per annum; and to increase them substantially for the more valuable premises. The maximum licence duty will now be $ 1,000 per annum instead of $ 250 per annum, but will apply only to premises the rental value of which is over $ 20,000 per annum. In the rural areas, where the only practicable basis is floor area, the licence duties will be increased by $ 5 to $ 12 per annum for the smaller shops of a floor area not exceeding 2,000 square feet and substantially (to a maximum of $ 50 per annum) for the larger shops.

It is proposed in the course of the year to rationalise and simplify the scheme of business licence duties generally, extending them with effect from next year to factories and to premises where services are supplied to the public.

A licence duty of $ 2,500 per annum will be imposed on all betting shops. This is the

first step towards a complete revision of the gambling laws and controls.

Duties are now levied on every conveyance or transport of immovable property at the rate of 1% *ad valorem*. It is proposed to raise the rate of duty to 2% *ad valorem*. Conveyances or transfers of other property (e.g. shares) are now dutiable at ¼% of the consideration or in the case of bonds, debentures, scrip, stock or shares, at ¼% of the face value. The rate will be increased to ½% and levied on the amount or value of the consideration in every case.

The capital gains tax, which is now levied at 15% only on short-term (not exceeding 7 years) gains, will be extended to long-term gains not exceeding 25 years from a commencing date not earlier than 1st January, 1960, at the rate of 10%.

Initial allowances, whereby 40% of the value of plant and machinery and 10% of the value of industrial buildings may be written off as depreciation initially for tax purposes, must be taken in the year immediately after the investment takes place or immediately after the end of the tax holiday period. It is proposed to permit these allowances to be spread over three years in any proportions the taxpayer wishes. This will have no long-run consequences for the revenue, but is expected to benefit the revenue in 1967 substantially.

The Government proposes to introduce legislation extending the period prior to death during which *inter vivos* transfers are exigible to estate duty, from three to five years.

Government is concerned at the wasted potential of idle land. It is considering the introduction of tax and incentive measures to encourage the productive use of land.

I should add that the Government proposes to examine the rate structure of the personal income tax with a view to decimalising it and correcting any anomalies or inequities.

In addition to these negative measures to increase the Government's take from the community, i.e. to shift income from your pockets into the public purse, the Government proposes to take further positive steps to accelerate the growth of the community's production and income so that, both directly from your own expenditure and indirectly through the Government's expenditure on community services, you may benefit from a higher level of income. It is only by making the national cake bigger than the community as a whole can benefit; taking a slightly bigger slice away from you by taxation is only a means to this end, but not an end in itself. Much more can be achieved by making the cake bigger.

With this objective in view, the Government will expand its development expenditure especially in directions which facilitate and stimulate private investment.

The Government has, with the assistance of the USAID, established a fund (the Private Investment Fund in the trusteeship of the Bank of Guyana) for financing industrial development. The fund will eventually build up to some $ 6.4 mn., available as it revolves for helping to finance worthy industrial projects. It is also proposed to set up a small fund whereby the Guyana Development Corporation can participate to some extent in new industrial developments. Thus, by helping on the finance side by loans through the P.I.F. and the Credit Corporation, by direct participation and by technical assistance, the Guyana Development Corporation will be enabled to fulfil its function of stimulating industrial development. The Guyana Development Corporation also proposes to increase the availability and liberalise the terms on which factory sites are provided on the industrial estates.

The pace of industrial development must be accelerated. The Government appreciates that it must demonstrate directly by its tax policy that it is prepared to maintain the right climate for investment. To this end, it is proposed to liberalise the present system of tax concessions in ways which I shall now discuss in general terms.

TAX HOLIDAYS. The present income tax concessions will be improved. The Government will offer, as an alternative to the present form of tax holidays, a tax holiday in the form of investment allowances whereby tax is waived by writing off for tax purposes at the beginning of their life a substantial proportion of the amount invested in fixed assets. This form has the advantage that the investor is assured that he will be allowed to recover a substantial proportion of his investment before his profits become exigible to tax. Provision will be made for extending the present five-year income tax holiday granted under the Income Tax (In Aid of Industry). Ordinance by a further period of up to five years where the Government is satisfied that the benefits received under the initial five-year tax holiday have not been adequate in the particular circumstances. It is also proposed to provide for the grant, without restriction, of a two-year tax holiday to any new approved secondary industry.

INITIAL ALLOWANCES. The range of industries eligible for initial allowances will be extended to include all secondary industry.

RAW MATERIALS FOR INDUSTRY. As a general policy, except where there are adequate local substitutes, provision will be made to the maximum extent practicable, for the duty-free importation of industrial raw materials, subject to the imposition, where necessary or advisable, of an excise or sales tax on local sales of the finished product.

PROTECTION TO INDUSTRY. The Government will continue its policy of granting reasonable protection to local industry against imports.

With the additional revenue measures yielding $ 5.4 mn., the deficit on the Current Estimates of $ 0.3 mn. will be converted to a surplus of $ 5.1 mn. The total budget will therefore show a surplus to $ 5 mn.

FISCAL AND FINANCIAL ORGANISATION

I have been trying ever since I assumed office to develop the fiscal organisation of the Government; to collect taxes efficiently; and to spend public funds economically and in the amounts and for the purposes for which they were provided. These are basic essentials to sound management of the Government's finances. Some progress has been made in these respects but we still have some way to go to achieve what is required. With the help of British Technical Assistance, which has supplied a specialist in training in Customs and Excise work, improved methods and procedures for collection of these taxes have been worked out and staff is being trained in their application. On a more practical and immediately rewarding plane, the campaign against bush rum has achieved considerable success. During the period 1st January to 30th November, 1966, 519 offences were detected; fines imposed by the Courts amounted to $ 83,025; 51 persons were sentenced to peremptory imprisonment; 31 cases are still pending; 437 stills were destroyed along with 794 gallons of the illegal spirits and 32,900 gallons of the wash. In the same period 258 persons were detected committing offences against the Customs

Laws. The total fines imposed during the year by the Courts together with compensation paid to the department, amounted to nearly $ 200,000.

On the Inland Revenue side, technical assistance is being arranged to provide the services of two experts; one to establish internal training arrangements; and the other to improve the organisation and methods for curbing tax evasion. Data processing equipment that will enable the accounting side of the department's work to be brought and kept up to date has been installed and will be in operation this year. With the expansion of the functions of the department and the growth in the number of taxpayers, the accounting system had become hopelessly inadequate for its purposes. Under the new system the entire process of billing taxpayers, tracking arrears, making refunds and accounting for tax receipts will be carried out by electronic methods. This will ensure prompt billing of taxpayers with full information about arrears and efficient tracking of the taxes due in relation to assessments. The next step—indeed the vital step—as I have indicated before, is to improve the assessment side. The main hindrance here is the shortage of professional staff. The department must be enabled to supply its own needs of skilled staff of this kind by setting up internal training arrangements and it must improve its methods for catching tax dodgers.

So much for the efficiency of tax collection. The other side of financial administration—adequate control and economy in the expenditure of public funds—has been a matter of great concern to me, as it should be to all of you. The whole system of parliamentary democracy is based on the premise that the Legislature can exercise adequate control over the expenditure of public funds. Indeed, even on the lower level of practical expediency, in order to mesh expenditures with the resources available for their financing, it is necessary that expenditures should be made to conform with the budgeted provision for them. The system of financial control must achieve this or fail the high ideals of the Constitution and the needs of practical finance. I must say that there are signs of a greater awareness of this need, but again we have some way to go in order to achieve what is required.

Part of the lack in this respect has been due to the inefficiency of the accounting system which failed to throw up quickly, and in sufficient detail, adequate expenditure figures. I have introduced with effect from this year a 'punched-card' (unit record) electro-mechanical accounting system which will provide prompt expenditure information and enable central tracking of the progress of expenditure.

However, this is only part of what is required. Ultimately, the effectiveness of the system will depend on the sense of responsibility which all those whose duty it is to expend public moneys show in their work. I hope to intensify the work of the Inspection Division of the Treasury to ensure that the methods and procedures required for expenditure control are carried out effectively and that accounts are paid promptly. I should also like to see the Public Accounts Committee functioning as it should this year.

Control, of course, while it is a vital part of sound financial administration, is not by itself sufficient. The public business must be organised in a way that ensures that public funds are spent economically. The spending departments must have the will and the Treasury must have the means, to ensure that the system of administrative control, especially through financial, accounting and stores procedures, is effective for ensuring that the work or service is executed economically

for its purpose. The Treasury must be in a position to test expenditure proposals by examining their proposed basis of execution to ascertain whether the public funds allocated to them are the minimum required to accomplish their purpose. Without such an organisation the Treasury can have no rational basis for pruning expenditure proposals to bring them within the bounds of the scarce funds required for their implementation. Last year the Organisation and Methods Division undertook the reorganisation and mechanisation of both the accounting and the stores systems.

Guyana joined the International Monetary Fund last year and has opted for full convertibility of its currency under Article VIII of the Articles of Agreement of the Fund. The economic stresses and strains of the past two years have proved the strength of its currency and justified this course. The free exchangeability of our currency since this Government took office has stimulated a welcome inflow of funds from abroad.

In the field of local financial institutions, 1966 saw the establishment of yet another commercial bank, the Bank of Baroda Limited, the second new commercial bank within two years to establish itself here— remarkable testimony to the rebirth of confidence in the future, especially when we consider that the number of commercial banks had been two for almost a century.

1966 saw an acceleration of the expansion of loans to the private sector from $ 30 million at the end of 1965 to $42 million at the end of November 1966. In the same period Savings Deposits in the commercial banks grew from $ 45 milllon to $ 50 million, with other deposits growing to a lesser extent.

1966 was the first year of the wider operations of our new Central Bank, the Bank of Guyana, which opened accounts for the commercial banks in March and took over the Government accounts in April. The Government's financial operations are now channelled through one bank which manages its bank accounts and supplies short-term credit on overdraft.

The Bank also furthered the progress of the market for Treasury Bills by buying and selling bills outside the monthly tender operations. At the end of last year $ 6.3 mn. in Treasury Bills was outstanding. A growing number of institutions and persons participated in this market, although thereis scope for further development as people become more familiar with this type of security. There was also some progress in respect of an improvement of the market for other Government securities. I am informed that the Bank of Guyana will soon enter into an agreement with institutions and persons active in the market for securities, for the exchange of information on prices and on offers for sales and purchases which will be published regularly—a first step towards a stock exchange in Guyana.

The progress made in respect of financial institutions in Guyana in recent years leaves us with the question of what further developments we should aim at. The question which comes first to mind is whether the existing institutions can meet the financial needs of the private industrial and agricultural development we are striving for. Here we must, of course, be careful not to lose sight of the fact that the mere establishment of such an institution does not provide the funds which can be utilised for its purpose nor the management to put them to good use. We have made progress in the direction of finding funds for industrial investment by setting up a Private Investment Fund under the trusteeship of the Bank of Guyana, from which loans can be made for medium and longer terms by commercial banks after consultation

with the Guyana Development Corporation. The Fund started somewhat slowly, which in part confirmed the impression that at the moment loan capital is not the main bottleneck for private industrial development.

The Credit Corporation has now completed a comprehensive stock-taking of its activities and loan cover with a view to assessing the resources available for further development of its functions. Since its establishment in 1954 $ 16 mn. in capital has been put into the organisation and $ 4 mn. lost or in jeopardy through bad and doubtful debts. While some such losses are inevitable in an institution of this kind, which must have an eye to development potential and not merely to financial security, high losses of this kind arising from unproductive use of these funds harm the economy by diverting real resources from productive use and drying up the fund which supports these loans.

In this context I feel that too much emphasis has been put on the housing sector of the Corporation's activities. I intend that this emphasis should shift substantially to primary and secondary industry. I should add that it is proposed to allocate funds which the Credit Corporation, on the recommendation of the Guyana Development Corporation can use for making small loans to artisans and the like. An allocation of funds will also be made for the purpose of stimulating agricultural development.

The Radio Bingo and the National Lottery are now well established. The public spent about $ ½ mn. on bingo tickets last year; and $ ¼ mn. on National Lottery tickets. These yielded about $ 100,000 in revenue which can be used for desirable hospital development. The Committee is to be congratulated on the successful organisation and administration of these schemes.

CONCLUSION

In brief, the budget for 1967 calls for expenditure—current and capital—of $ 128.6 mn. This is $ 12.7 mn. more than in 1966—an increase of nearly 10%. With the revenue measures I have outlined, the funds in sight for financing this expenditure total $ 133.6 mn. There will therefore be a surplus of $ 5.0 mn. to help liquidate some of the short-term indebtedness ($ 17 mn. at the end of 1966).

The progress in the last two years is heartening. But we have yet a long way to go. And it will not be an easy way. There will have to be sustained and conscientious effort if the country is to realise its potential for development. There are few who would dispute with me when I say that the country's production can be increased by better co-operation between labour and capital. We must produce more efficiently both in agriculture and industry. We must discard our prejudices against articles of local manufacture. Buying local products is one of the ways in which we can help our country to progress.

I have had ample evidence of the willingness of people to change their ways and work for a better future. Many have brought me ideas and given me support without my asking.

There have been disappointments in the public service, but there have been many encouragements. I am satisfied that, in spite of the difficulties under which public officers work, there is a genuine will to serve their country.

Pride in our new country and its independence is not confined to the Public Service. Many firms and individuals, both inside and outside the country, have demon-

strated their interest in Guyana's future by making gifts to mark the occasion of independence. I take this opportunity to thank them publicly on behalf of the Government. One thing this year of independence has shown—that there is a fund of goodwill in the outside world for Guyana. The support—both in finance and technical assistance—we receive from our friends in Canada, Germany, the United Kingdom and the United States, and also the United Nations and its specialised agencies, we gratefully acknowledge.

What then is the prospect which faces the newly independent territory of Guyana? There are those who say that it is in the grip of stagnation, that the policies pursued by the present government are doing little to advance it towards progress and prosperity. These prophets of doom have already been routed on another front: their predictions of a $ 10 mn. current deficit in 1966 are slightly off the mark. The 1966 current budget has shown, not a deficit, but a surplus. They would have done better to have followed the technique of the ancient Oracle of Delphi.

The facts are indicative of optimism and not pessimism. Never in the history of this country has the outlook for the future been better. We see a stable and peaceful country; we see signs everywhere of a substantial injection of capital and an expansion of employment; we see many new buildings going up; we see new industries budding in a favourable climate for investment; we see new roads being built; we see a zest for knowledge and skills.

All these add up to a tremendous development and potential for further development. If these favourable factors can be joined with more efficient administration, greater productivity, stricter financial discipline and united effort, then independent Guyana would be well on the highway to prosperity.

Body of Laws on Direct Taxation in the Somalian Republic

(an extract)
of November 5, 1966

SUPPLEMENT TO THE BULLETIN FOR INTERNATIONAL FISCAL DOCUMENTATION
AU BULLETIN DE DOCUMENTATION FISCALE INTERNATIONALE

Vol XXI, No. 7/8, July-August/juillet-août 1967

INTERNATIONAL BUREAU OF FISCAL DOCUMENTATION

Muiderpoort - 124 Sarphatistraat - Amsterdam

The body of laws on direct taxation in the Somalian Republic was approved on November 5, 1966. This legislative decree came into force on January 1, 1967.

TEXT

PART I: INCOME TAX

TITLE I

GENERAL PROVISIONS

CHAPTER I: IMPOSITION OF TAX

Article 1

Territorial applicability of the tax

Income tax shall be charged upon income accruing or received in the Territory of the Republic.

Article 2

Basis of assessment

Income tax shall be charged upon the income, accruing or received, in cash or in kind, whether of a permanent or of an occasional nature deriving from capital or work or both or from any other source.

Article 3

Period in respect of which tax is payable

Income tax shall be payable for the period during which the chargeable income accrues or is received.

Article 4

Prohibition to charge tax more than once upon the same income

Income tax shall not be charged more than once upon the same income, even in the name of different persons.

Article 5

Year of assessment

1. For the purposes of income tax, the year of assessment shall commence on 1 January and end on 31 December in each year.
2. Income tax shall be charged, for each year of assessment, upon the aggregate amount of the net income of the person assessed, accruing or received during the year preceding the year of assessment.
3. The year preceding the year of assessment shall be the calendar year in which the chargeable income accrues or is received.
4. Where the financial year of a company or association assessable on the basis of its balance sheet does not coincide with the calendar year, the year of assessment in respect of that company or association shall be the year in which the balance sheet is made up in accordance with law or by-laws.
5. The aggregate amount of the net income referred to in the previous paragraphs shall constitute the chargeable income of the person assessed.

CHAPTER II: PERSONS ASSESSABLE

Article 6

Persons assessable

1. Income tax shall be charged in the name of physical or juridical persons, whether public or private.
2. Where the person assessable is an alien or a company or association established abroad, income tax shall be charged upon that portion of income which accrues or is received in the Territory of the Republic.

Article 7

Chargeability of husband and wife

1. Husband and wife shall pay the income tax separately, on the basis of their respective incomes.
2. Where husband and wife are the holders of separate trade licences, and the respective activities are carried on at the same premises, their incomes shall be consolidated, and the tax shall be charged in the name of the spouse carrying on the prevailing activity.

Article 8

Chargeability of representatives of incapacitated persons and persons not resident in the Territory

1. A minor or incapacitated person shall be assessable and chargeable to tax in the name of his legal representative.
2. A person not resident in the Territory shall be assessable and chargeable to tax in the name of his trustee, guardian, curator or committee or of any attorney, factor, agent, receiver, branch or manager, in respect of any income arising, whether directly or indirectly, through or from any attorneyship, factorship, agency, receivership, branch or management.

Article 9

Obligations of persons assessable and legal representative absent from, or not resident in the Territory

1. A person or his legal representative who absents himself from, or does not reside in the Territory of the Republic shall for purposes of compliance with the fiscal obligations referred to in this Decree, appoint a representative in the Territory and notice such appointment in writing to the competent office which may request the deposit of a suitable security for the payment of the tax.
2. Where any such person or legal representative fails to appoint a representative or notify the appointment, the competent office shall notify any ascertainment, additional assessment other notice by posting it for thirty consecutive days on the notice board of the Local Administration or District offices of one of the localities indicated in Art. 29, para 1.
3. The Local Administration or District office shall certify the posting in the return of the notification.

Article 10

Responsibility of legal representatives

The legal representative of a minor, incapacitated person and corporate bodies of persons shall be responsible, under the terms of this decree, for the ascertainment and assessment of the income received by the person represented by him. He shall also be responsible for the payment of the tax, within the limits of the estate of the person represented.

Article 11

Responsibility of heirs

1. In the case of death of the person assessable, his heirs, personal representative, or custodian of the estate in abeyance or of the estate accepted without liability to debts beyond the assets descended, shall submit the return of the income in the year of assessment following the year in which the death occurred, and shall perform any other act prescribed by this Decree.
2. The personal representative and the custodian of the estate in abeyanc or of the estate accepted without liability to debts beyond the assets descended, shall also be responsible, within the limits of the deceased's estate for the payment of the tax due in respect of the years preceding the year of death, in accordance with the ascertainments made by the competent office or with the adjustments of returns.

CHAPTER III: CHARGEABLE INCOME

Article 12

Chargeable income

1. Except as otherwise provided by this Decree, income tax shall be charged upon the following incomes accruing or received in the Territory of the Republic:
a) profits from any industrial, commercial, professional or vocational activities, irrespective of the duration of such activity;
b) interest or discounts, charges or annuities, rents and royalties;
c) occasional and extraordinary gains and any other income of any nature whatsoever deriving from other sources;

d) agricultural incomes;
e) real or presumed incomes from buildings and from any other permanent structure, even if used by the owner and on his behalf or by another for the purpose of residence or enjoyment, and not for the purpose of gain;
f) pensions and income from employment, of any nature whatsoever, paid under the terms of a contract of employment.

2. Special Local Administration taxes shall be charged upon the real or presumed incomes in respect of constructions of a traditional and local character, and the agricultural incomes derived from cultivation of land by traditional and local systems.

Article 13

Income from contracts and similar sources

Income derived from contracts for works or supplies, trustéeships, guardianships, and, similar sources, whose duration exceeds one calendar or financial year, shall be calculated on the basis of the profit received and expenses incurred in respect of the activity carried on in the year preceding the year of assessment, taking into account the risk involved in the activity.

Article 14

Income from industrial buildings

1. Income tax shall be jointly charged upon the income from buildings and other permanent structures used for the purpose of carrying on an industrial activity, and upon the income derived from such industrial activity, provided that the industrial activity is directly carried on by the owner of the building.

2. Where the industrial activity is not directly carried on by the owner of the building, the income tax shall be charged upon the rent at the rate provided for the tax on the income from buildings.

CHAPTER IV: EXEMPTIONS

Article 15

Persons exempt from income tax

The following shall be exempt from income tax:

a) the President of the Republic, in respect of his annual emoluments;
b) the State and Local Administrations;
c) international organizations and bodies, in conformity with the generally accepted rules of international law and international treaties binding on the Republic;
d) diplomatic agents of foreign States, in respect of their salaries and any other emolument received in connection with their functions;
e) consular agents of foreign States, in respect of their salaries and any other emolument received in connection with their functions;
f) officials and employees of the United Nations and its specialized Agencies and of foreign and international organizations and bodies, in conformity with international agreements, in respect of their salaries and any other emolument received in connection with their functions;
g) members of the Armed Forces and parmilitary organizations below the rank of non-commissioned officer, on active duty, in respect of their salaries and emoluments;

h) lawfully established charitable and welfare institutions, bodies and foundations; educational institutions; institutes, academies and societies having exclusively cultural purposes; religious institutions— provided that income derived from any commercial activity shall be excluded from exemption;
i) companies, societies and bodies which are the holders of mining or oil concessions, where the concession agreement approved in the manner prescribed by law provides for the payment of direct taxes inclusive, or in lieu, of income tax.

Article 16

Income permanently exempt from tax

Income tax shall not be charged upon the following:
a) buildings used for public worship, and their appurtenances;
b) cemeteries and their appurtenances;
c) State owned buildings;
d) buildings, housing foreign embassies, legacies or consulates, provided such buildings are the property of the States represented by such embassies, legacies or consulates;
e) buildings used as schools, including private schools, provided such schools are organized on a non-profit basis and are authorized by the Ministry of Education;
f) buildings owned by the United Nations and its specialized Agencies, or by international organizations or bodies;
g) rural buildings belonging to the owner or concessionary of the land, provided they are used for the purpose of residence by those who personally cultivate the land, where the value of the building does not exceed Sh. So. 10,000*); or for the purpose of housing animals bred on the land; or for the purpose of storage and primary processing of the agricultural products or safe-keeping and preservation of machinery, equipment and other materials used for the cultivation of the land;
h) 40% of the undistributed profit of industrial enterprises technically organized and assessable on the basis of their balance sheet, provided such profit is clearly shown in a reinvestment fund entered in the liability side of the balance sheet, and does not exceed 25% of the chargeable income. Income tax shall be charged upon any disbursement of profit undistributed and set aside in the reinvestment fund;
i) dividends on shares, and interests on postal bonds and deposits;

Article 17

Temporary exemptions in favour of industrial or agricultural enterprises

1. The Minister of Finance may, as an exceptional measure, and for a period not exceeding 10 years, wholly or partly exempt new industrial or agricultural enterprises from income tax, on the proposal of the Minister of Industry and Commerce as regards industrial activities or on the proposal of the Minister of Agricultural and Animal Husbandry as regards agricultural activities.
2. The exemption shall only be granted where the enterpriser concerned proves that he will run an extraordinary risk and that he will either produce new goods or, in producing goods, will use a more advanced technique which was not previously used.
3. Exemption shall also be granted where the enterpriser proves that he will run an extraordinary risk in carrying on industrial or agricultural activities which, without involving any actual processing of goods, preserve or condition such goods thereby increasing their economic value.
4. Exemption shall also be granted to enter-

*) 7.143 So. Sh. per US$ (editor's note)

prisers who enlarge or radically renovate existing enterprises, provided that the conditions mentioned in paragraphs 2 and 3 of this article are fulfilled.

5. An enterpriser who can prove that he produces the same goods or uses the same technique as another enterpriser to whom exemption from income tax has already been granted, may be exempt from income tax under conditions not more favourable than those granted to the other enterpriser. Such exemption shall expire on the date on which the exemption granted to the other enterpriser expires.

6. This exemption shall only be granted in respect of income not exceeding 10% of the invested capital and only for the period which, in the opinion of the Minister of Finance, will be required for the amortization of the invested capital.

7. New technically organized industrial enterprises which, according to Art. 17 of the Income Tax Law N. 15 of 16 November 1957, are already exempt from income tax, shall continue to be exempt from income tax upto a maximum of 10% of the invested capital and for a period not exceeding 10 years from the date on which they become useable.

8. For the purpose of Art. 17 of Law N. 15 of 16 November 1957 and of this Decree, the expression 'new technically organized industrial enterprises' means industrial enterprises consisting of a complex of goods, machinery, and equipment intended for the carrying on, on a permanent basis, of a industrial activity organized in accordance with strictly technical principles for the purpose of producing or processing raw materials or manufactured articles, or any other industrial activity which, without involving any actual processing of goods, preserves or conditions such goods thereby increasing their economic value.

CHAPTER V: DEDUCTIONS

Article 18

Expenses and liabilities

1. For the purpose of ascertaining the net income of any person, there shall be deducted all liabilities and expenses incurred by such person in the production of the income.

2. There shall also be deducted all interests payable to persons having their domicile or residence in the national territory, or permanently carrying on their activity therein.

Article 19

Losses

For the purpose of ascertaining the net income of an enterprise there shall be deducted any loss incurred by reason of the total or partial destruction of the property pertaining to the enterprise, or of the sale of such property at a price lower than the portion of costs which has not yet been written off.

Article 20

Operating deficits

1. Companies and associations assessable on the basis of the balance sheet may deduct the amount of the operating deficits relating to a financial year from the income of the subsequent financial years, for a period not exceeding three years.

2. The provision of the previous paragraph shall apply also to persons who are not assessable on the basis of a balance sheet, provided that the income of the three years preceding the year in which the deficit occurs has been ascertained on the basis of book entries kept in accordance with the regulations in force, and provided also that the income of the years in respect of which the deduction is allowed is ascertained in the same manner. The deficit shall be ascertained in accordance with the provisions concerning the ascertainment of income.

Article 21

Depreciation

1. The annual rates of depreciation in respect of the wear and tear of movable and immovable property, plants and machinery, patent and concession rights, trademarks and other property subject to depreciation, shall be allowed as a deduction.
2. The rates of depreciation shall be reasonably proportioned to the duration of the property concerned.

Article 22

Gratuities Fund

1. Any amount yearly and voluntarily set aside in a fund for the payment of gratuities and other benefits relating to termination of service in accordance with the provisions on private employment contracts and collective labour agreements shall be yearly deducted from the gross income, provided that they are shown in a special account entered in the liability side of the balance sheet, of which an annual statement is made, verified by the Direct Taxation Office, and provided also that they are placed in appropriate passbooks at a bank.
2. The amount of such fund shall be determined in relation to the legal position of the personnel employed in the business.
3. Any out-payment made for purposes other than those for which the special fund was formed, shall be assessable.

Article 23

Deductions in respect of the gross income from buildings

The net income from buildings and structures referred to in Art. 12 (e) shall be calculated by deducting from the gross income an amount equal to 20% of such income for repairs, maintenance, and any other expense or loss which might have been incurred.

Article 24

Deductions not to be allowed

No deduction shall be allowed in respect of.

a) domestic or private expenses;
b) any loss, diminution, exhaustion or withdrawal of capital, any sum employed as capital, or any expenditure for a capital purpose;
c) any loss or expense which is recoverable under any insurance, contract or indemnity;
d) rent of any buildings or part of buildings not paid for the purpose of producing the income;
e) any interest on the owner's capital;
f) remuneration for work done by the person assessable, or by his spouse, children and relatives up to the third degree who are employed in the business, provided they live together with the person assessable;
g) remuneration of directors of companies or associations assessable on the basis of their balance sheet.

CHAPTER VI: RETURN

Article 25
Obligation to furnish returns of income

1. Except as otherwise provided in Art. 30, every person chargeable with income tax shall furnish a return of the income in respect of which he is chargeable.
2. A single return shall be furnished for all the incomes of the person chargeable.
3. The return of the income of minors, incapacitated persons, corporated bodies of persons, and persons absent from or not resident in the Territory, shall be furnished by their representatives according to the provisions of this Decree.
4. The return may be furnished by an attorney of the person chargeable. The attorneyship shall be proved by a written document, even in the form of a letter, and shall be attached to the return.

Article 26
Return of income of associations not having legal personality

1. The returns of income of associations not having legal personality shall be furnished by the individual members in respect of the portions of income pertaining to them.
2. The competent office may request the legal representative of the association or any member thereof resident in the national territory to furnish the return.
3. Where the members are absent from or not resident in the Territory, the return shall be furnished by the attorney, factor, agent, receiver, or manager of the association.

Article 27
Time-limit within which returns are to be furnished

1. The returns of income shall be furnished within 31 March in each year.
2. Companies and associations assessable on the basis of the balance sheet shall furnish the return within one month after the approval of the balance sheet or statement of accounts. Where the balance sheet or statement of accounts is not approved within the time-limit prescribed by law or by-laws, the return shall be furnished within one month after the expiry of such time-limit.
3. In case of incorporation or, merger of companies or associations assessable on the basis of the balance sheet, the return, accompanied by the closing balance sheet of the company or association which has ceased to exist, shall be furnished by the incorporating company or association or by the company or association resulting from the merger, within three months after the date on which the deed of incorporation or merger has been signed.
4. Where a company or association is liquidated, the liquidators shall furnish a return of the residual income within three months after the deposit of the final balance sheet.

Article 28
Contents and signing of the return

1. The return shall indicate, for each item of income, the source, the gross profits, the expenses, the liabilities which can be deducted, the net income, and the particulars of the receipt proving the payment of the Government surtax referred to in Chapter IX of this Title.
2. In order to be valid, the return shall be signed by the person chargeable with income tax or by his legal representative.

Article 29
Returns to be furnished to the competent offices, etc.

1. The returns of income shall be furnished

to the Direct Taxation Officé, or to the Regional Revenue Offices or to the offices of the District in which the person assessable resides, has his registered office, or carries on his prevailing activity.

2. The return may also be sent by mail, as a registered letter with return receipt.

3. The receipt issued by the competent office or the receipt for the registered letter shall be the only evidence that the return has been furnished.

Article 30

Exemption from the obligation to furnish the return of income

A person whose income does not exceed Sh. So. 3,000 shall be exempt from furnishing the return of income, provided he has paid the Government surtax and the Local Administration tax on trade licences according to the provisions of Chapter IX, and provided also that the exemption shall be granted only in respect of the income from that trade.

CHAPTER VII: INCOME FROM EMPLOYMENT

Article 31

Income tax to be paid by employer

1. The income tax chargeable upon the income from employment referred to in Art. 12 (f) shall be paid by the physical of juridical persons, whether public or private, who employ the persons receiving such income. The employers shall recover the amount of the tax from the persons employed by them.
2. The amount of the tax shall be recovered by deducting it from the salary or wages paid to the employee, at the rates indicated in Art. 37.
3. Where the amount of the tax is not recovered as indicated above, the tax shall be collected again in the name of the employee.

Article 32

Travel allowance

Travel and mission allowances paid without rendering of account, and wages and victuals paid to seamen shall be assessable to the extent of 40% of their amount.

Article 33

Seniority and social security allowances

1. Seniority and social security allowances paid upon termination of service shall be exempt from income tax, provided their total amount divided by the number of years of service gives a quotient not exceeding Sh. So. 200.
2. Where the quotient exceeds Sh. So. 200. - the income tax shall be charged in the same manner provided for salaries and wages.

Article 34

Deductions

1. Contributions for social security which, according to law or collective agreements, are paid by workers, shall be allowed as a deduction from the income from employment.
2. Contributions for social security which, according to law or collective agreements, are paid by employers, whether or not they are proportioned to the worker's remuneration, shall not be deemed to be a part of the assessable income.

Article 35

Payment of tax and liability of employers

1. The return of the incomes referred to in this Chapter shall be furnished, and the income tax shall be paid quarterly, within the month followlng each quarter, to the Direct Taxation Office, or Regional Revenue Offices, or District Offices.

2. Income tax charged upon a civil servant shall be directly collected by the State by deducting the corresponding amount from the salary or other emolument of any nature whatsoever paid to the civil servant.

3. Employers who are required to pay the tax and to recover the corresponding amount or directly deduct it from the emoluments paid to their employees under the terms of the previous paragraphs, shall be personally liable for the payment of the tax.

CHAPTER VIII: RATES OF TAX

Article 36

Rates of tax on income from buildings

The income from buildings referred to in Art. 12 (e) and Art. 23 shall not be assessed together with the income from any other source, and the income tax shall be separately charged upon it at he following rates:

upto Sh. So. 30,000	rate 15 %
on the part exceeding Sh. So. 30,000	rate 22,50%

Article 37

Rates of tax on income from employment

The yearly income from employment and pensions referred to in Art. 12 (f) shall not be assessed together with the income from any other source, and the income tax shall be separately charged upon it at the following rates:

income up to Sh. So. 2,400							exempt
on the part exceed.	Sh. So.	2,400	upto	Sh. So.	9,600		rate 6%
on the part exceed.	Sh. So.	9,600	upto	Sh. So.	18,000		rate 12%
on the part exceed.	Sh. So.	18,000			,		rate 18%

Article 38

Rates of tax on income from buildings

1. Income tax shall be charged upon the total chargeable income from the sources referred to in Art. 12 (a), (b), (c), (d), at the following rates:

income up to Sh. So. 2,400							exempt
on the part exceed.	Sh. So.	2,400	upto	Sh. So.	3,600		rate 9%
on the part exceed.	Sh. So.	3,600	upto	Sh. So.	4,800		rate 11%
on the part exceed.	Sh. So.	4,800	upto	Sh. So.	6,000		rate 13%

on the part exceed.	Sh.	So.	6,000	upto	Sh.	So.	7,200		rate 15%
on the part exceed.	Sh.	So.	7,200	upto	Sh.	So.	8,400		rate 17%
on the part exceed.	Sh.	So.	8,400	upto	Sh.	So.	9,600		rate 19%
on the part exceed.	Sh.	So.	9,600	upto	Sh.	So.	10,800		rate 22%
on the part exceed.	Sh.	So.	10,800	upto	Sh.	So.	18,000		rate 25%
on the part exceed.	Sh.	So.	18,000	upto	Sh.	So.	30,000		rate 28%
on the part exceed.	Sh.	So.	30,000						rate 30%

2. Rate of tax to be paid by juridical persons:
Chargeable income of any amount rate 30%

Article 39

Rates of Local Administration additional tax

1. An additional tax shall be paid in favour of Local Administrations, and its amount shall be equal to one sixth of the amount of the income tax.
2. The additional tax shall be equal to one twentieth of the income tax, in respect of income from employment referred in Art. 12 (f).
3. The additional tax shall be collected by the Direct Taxation Office together with the income tax, and shall be indivisible.
4. The office, upon collection of the additional tax, shall pay it in to the Local Administration in whose territorial jurisdiction the taxpayer has his registered office or carries on his prevailing activity, and the Local Administration shall issue a payment receipt to be attached to the monthly accounts.

CHAPTER IX: GOVERNMENT SURTAX ADDITIONAL TO THE LOCAL ADMINISTRATI ON TAXON TRADE LICENCES

Article 40

Government Surtax

A Government surtax, additional to the Local Administration Tax on trade licenses, shall be paid upon the granting or renewal of trade licences.

Article 41

Government surtax to be paid in lieu of, or to be deducted from income tax

1. The Government surtax paid under the terms of the previous article shall be deemed to be paid in lieu of the income tax in respect of the following income produced in the year in which the licence is granted or renewed:
   a) real and actual income whose amount is lower than Sh. So. 3,000;
   b) real and actual income in respect of which the amount of the income tax, calculated as prescribed in Art. 37, is equal to or lower than the amount of the Government surtax paid upon the granting or renewal of the licence.
2. In any other case, the competent office shall deduct the amount of the Government surtax paid under the terms of the previous paragraph from the amount of the income tax to be paid on the basis of the return or ascertaiment.

Article 42

Rates of the Government surtax

1. The rates of the Government surtax referred to in Art. 40. to be paid in respect of trade licences granted or renewed by the Local Administrations, shall be as follows:

Licence of I	Category Surtax Sh. So.	300.–
Licence of II	Category Surtax Sh. So.	200.–
Licence of III	Category Surtax Sh. So.	150.–
Licence of IV	Category Surtax Sh. So.	100.–
Licence of V	Category Surtax Sh. So.	40.–
Licence of VI	Category Surtax Sh. So.	20.–
Licence of VII	Category Surtax Sh. So.	50.–

2. The Government surtax shall be collected together with the Local Administration additional tax referred to in Art. 39.

Art. 43 - Art. 120:

Ascertainment, Appeals, Collection of the Tax, Compulsors execution, Penalties; not printed here

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PART II: TAX ON COMPANIES' CAPITAL

Article 121

Territorial applicability of the tax

The tax on companies' capital shall be charged upon the capital of juridical persons operating in the territory of the Republic.

Article 122

Basis of assessment

The tax shall be charged upon the chargeable capital of the persons assessable.

Article 123

Persons assessable

The tax shall be charged in the name of all juridical persons, including those exempt from income tax, assessable on the basis of the balance sheet and of foreign companies, bodies of persons and associations operating on a permanent basis in the territory of the Republic.

Article 124

Chargeable capital

1. For the purpose of the tax on companies' capital the chargeable capital shall include:

a) the subscribed and paid-up capital of companies or net assets of other associations or bodies of persons, as shown in their balance sheet and statement of accounts;
b) ordinary and extraordinary reserves of any nature whatsover, as shown in the balance sheet or statement of accounts, excluding reserves set aside for the purpose of meeting specific commitments and liabilities, or on behalf of third parties;
c) profits carried forward from the previous financial year.

2. Any loss carried forward from the previous financial years shall be deducted from the

total chargeable capital referred to in the previous paragraph.

3. The chargeable capital of foreign companies, bodies of persons and associations shall include any capital to be invested in their operation within the territory of the Republic, or any capital actually invested where this is higher than the capital intended for such investment. In this case, the chargeable capital shall never be lower than the chargeable income capitalized at 100 by 10.

Article 125

Rate of tax

The tax shall be charged at the rate of 0,50% upon the chargeable capital as determined in accordance with the previous article.

Article 126

Year of assessment

The year of assessment shall commence on 1 January and end on 31 December in each year.

2. In respect of each year of assessment, the tax shall be charged:

a) upon the chargeable capital as shown in the balance sheet or statement of accounts closed on 31 December in the year preceding the year of assessment;
b) upon the chargeable capital as shown in the balance sheet or statement of accounts closed on 31 December in the year of assessment.

Article 127

Exemptions

1. The following shall be exempt from the tax:

a) cooperative societies and stores, provided they are organized in accordance with cooperative principles;
b) Local Administrations, Chambers of Commerce, and State or Municipal companies providing, on a monopoly basis, services of public interest;
c) bodies engaged in reclamation works, land improvement, irrigation, and water works;
d) charitable and religious institutions, public bodies providing social security and welfare services, and other bodies established for charitable or educational purposes;
e) educational institutions established on a non profit basis;
f) bodies, companies and institutions which, by law or under any international treaty, are exempt from taxation.

2. No exemption shall be granted in respect of any activity carried on by the aforesaid companies, bodies or institutions, for profit purposes.

Article 128

Return — Ascertainment — Appeals Collection — Penalties

The return of chargeable capital, ascertainment, appeals, collection, and penal and administrative penalties shall be governed by the provisions of Part I of this law, insofar as applicable.

PART III: Tax on Slaughtered Animals
not printed here

PART IV:

FINAL AND TRANSITIONAL PROVISIONS

Article 135

International agreements

The Government of the Republic may conclude international agreements with the Governments of other Countries, on condition of reciprocity, for the purpose of not having the same direct tax levied more than once.

Article 136

Franking

Any correspondence between officers in the financial administration, public offices and taxpayers, exchanged in the exclusive interest of the tax service, may be franked, provided it bears the frank supplied by the post administration.

Article 137

Official secret

Any information regarding the assessment of tax and disputes relating thereto, supplied without an order of the Court by personnel in the financial administration to persons not belonging to such administration other than the person assessed or his representative, shall be considered as violation of official secret.

Article 138

Applicability of enforcement proceedings

The enforcement proceedings provided for in Chapter II Title IV, shall be applicable to all taxes of the State and to all proceedings pending on the date of entry into force of this Legislative Decree.

Article 139

Regulations and list of the taxpayers

1. The Minister of Finance may issue regulations for the proper implementation of this Body of Laws and for the inspection and registration of buildings and other masonry constructions.

2. The Minister of Finance shall publish yearly a list of taxpayers showing the returned income and the amount of the tax due.

Convention between the government of the United States of America and the government of the United States of Brazil for the avoidance of double taxation with respect to taxes on income

SUPPLEMENT TO THE BULLETIN FOR INTERNATIONAL FISCAL DOCUMENTATION
AU BULLETIN DE DOCUMENTATION FISCALE INTERNATIONALE

Vol XXI, No. 10, October/octobre 1967

INTERNATIONAL BUREAU OF FISCAL DOCUMENTATION

Muiderpoort - 124 Sarphatistraat - Amsterdam

On March 13, 1967, representatives of the Brazilian and United States Governments concluded a tax treaty to avoid double taxation between the two countries. The text of this treaty is published infra. The treaty has not yet been ratified. We hope to publish a commentary on this important treaty in a coming issue of the Bulletin.

TEXT

The Government of the United States of America and the Government of the United States of Brazil desiring to conclude a convention for the avoidance of double taxation with respect on income,
Have agreed as follows:

Article 1

Taxes Covered

1. The taxes which are the subject of the present Convention are:
a) In the case of the United States of Brazil, all taxes covered by the Federal Income Tax Law applicable to individual taxpayers and legal persons which may result from the application of Brazilian Income Tax regulations, except for the tax imposed under Article 295 (tax on activities of minor importance) and Article 299 excess (remittance tax) of the Brazilian Income Tax Regulations consolidated by Decree No. 58,400 of May 10th, 1966 (hereinafter called "Brazilian tax").
b) In the case of the United States of America, the Federal income tax, including surtax, but not including the taxes imposed under section 531 (improperly accumulated earnings tax) and section 541 (personal holding company tax) of the Internal Revenue Code (hereinafter called "United States tax").

2. The present Convention shall also apply to taxes substantially similar to those covered by paragraph (1) of this Article which are subsequently imposed in addition to, or in place of, existing taxes.

3. For the purpose of Article 6, this Convention shall also apply to taxes of every kind, and those imposed at the national, state, or local level.

Article 2

General Definitions

1. In the present Convention, unless the context otherwise requires:

a) The term "Brazil" means the United States of Brazil;

b) The term "United States" means the United States of America, and when used in a geographical sense means the States thereof and the District of Columbia;

c) The terms "one of the Contracting States" and "the other Contracting State" mean Brazil or the United States as the context requires;

d) The term "tax" means Brazilian tax or United States tax as the context requires;

e) The term "person" comprises an individual, a corporation and any other body of individuals or persons;

f) The term "corporation" or "company" means any body corporate, association or joint stock company or other entity which is treated as a body corporate for tax purposes;

g) The term "United States corporation" or "corporation of the United States" means a corporation which is created or organized under the laws of the United States or any State thereof or the District of Columbia;

h) The term "Brazilian corporation" or "corporation of Brazil" means a company, as defined in subparagraph (1) (f) of this Article, created or organized under the laws of Brazil and maintaining its administrative headquarters in Brazil;

(i) The term "resident of one of the Contracting States" means an individual who is a resident of that Contracting State for purposes of the tax of that Contracting State and includes an individual acting as a partner or fiduciary to the extent that the income derived by such individual in that capacity is taxed as the income of a resident;

j) The terms "resident or corporation of one of the Contracting States" and "resident or corporation of the other Contracting State" mean a resident or corporation of Brazil or a resident or corporation of the United States, as the context requires;

k) The term "competent authority" means:

(i) in Brazil, the Minister of Finance or his authorized representatives;

(ii) in the United States, the Secretary of the Treasury or his delegate.

l. The term "State" means any national State, whether or not one of the Contracting States.

2. As regards the application of the present Convention by a Contracting State, any term not otherwise defined shall, unless the context otherwise requires, have the meaning which it has under the laws of that Contracting State relating to the taxes which are the subject of the present Convention.

Article 3

General Rules of Taxation

1. A resident or corporation of one of the Contracting States shall be taxable by the other Contracting State only on income derived from sources within that other Contracting State. For this purpose, the rules set forth in Article 5 shall be applied to determine the source of income.

2. A resident or corporation of one of the Contracting States may be taxed by the other Contracting State on income taxable under paragraph (1) only in accordance with

the limitations set forth in the present Convention. Any income to which the provisions of the present Convention are not expressly applicable shall be taxable by each of the Contracting States in accordance with its own law. The provisions of the present Convention shall not be construed to restrict in any manner any exclusion, exemption, deduction, credit or other allowance now or hereafter accorded (a) by the laws of one of the Contracting States in the determination of the tax imposed by that State or (b) by any other agreement between the Contracting States.

3) Except as provided in paragraph (4) of this Article, a Contracting State may tax an individual who is a citizen or resident of that Contracting State (whether or not such person is also a resident of the other Contracting State) or a corporation of that Contracting State as if the present Convention had not come into effect.

4. The provisions of paragraph (3) shall not affect—

a) the benefits conferred by a Contracting State under Articles 4 (Relief from Double Taxation) and 6 (Nondiscrimination);

b) the benefits conferred by the United States under Articles 7 (Investment Credit) and 22 (Deduction for Charitable Contributions); and

c) the benefits conferred by a Contracting State under Articles 18 (Teachers), 19 (Students and Trainees), 20 (Governmental Salaries), and 21 (Rules Applicable to Personal Income Articles) upon individuals, other than citizens of, or individuals having immigrant status, in that Contracting State.

Article 4

Relief from Double Taxation

Double taxation shall be avoided in the following manner:

1. The United States shall allow to a citizen, resident or corporation of the United States as a credit against its tax specified in subparagraph (1) (b) of Article 1 the appropriate amount of taxes paid to Brazil and, in the case of a United States corporation owning at least 10 percent of the voting power of a corporation resident in Brazil, shall allow credit for the appropriate amount of taxes paid to Brazil by the corporation paying such dividends with respect to the profits out of which such dividends are paid. Such appropriate amount shall be based upon the amount of tax paid to Brazil but shall not exceed that proportion of the United States tax which net income from sources within Brazil bears to the entire net income. For the purpose of applying the United States credit in relation to taxes paid to Brazil, the rules set forth in Article 5 shall be applied to determine the source of income.

2. Brazil shall allow to a resident or corporation of Brazil as a credit against its tax specified in subparagraph (1) (a) of Article 1 the appropriate amount of taxes paid to the United States and, in the case of a corporation of Brazil owning at least 10 percent of the voting power of a United States corporation, shall allow credit for the appropriate amount of taxes paid to the United States by the corporation paying the dividends with respect to the profits out of which such dividends are paid. Such appropriate amount shall be based on the amount of tax paid to the United States but shall not exceed that proportion of Brazilian tax which net income from sources within the United States bears to the entire net income subject to Brazilian tax. For the purpose of applying the Brazilian credit in relation to taxes paid to the United States, the rules set forth in Article 5 shall be applied to determine the source of income.

Article 5

Source of Income

For purposes of Articles 3 and 4:

1. a) Except as provided in subparagraph (b)—

(i) dividends paid by a corporation of one of the Contracting States shall be treated as income from sources within that Contracting State; and

(ii) dividends paid by any other corporation shall be treated as income from sources outside that Contracting State.

b) Dividends paid by any corporation shall be treated as income from sources within a State if such corporation—

(i) had a permanent establishment in that State, and

(ii) derived more than 85 percent of its gross income from sources within that State

for a three-year period ending with the close of its taxable year preceding the declaration of such dividends (or for such portion of that period as the corporation has been in existence).

2. a) Except, as provided in subparagraph (b), interest paid by a Contracting State, including any local government thereof, or by resident or corporation of that Contracting State shall be treated as income from sources within that Contracting State; and interest paid by any other person shall be treated as income from sources outside that Contracting State.

b) Interest paid by a resident or corporation of any State with a permanent establishment in another State directly out of the funds of such permanent establishment on indebtedness incurred for the sole use of, or on banking deposits made with, such permanent establishment shall be treated as income from sources within the State in which such permanent establishment is located.

3. Royalties paid by a resident or corporation of one of the Contracting States for the use of, or the right to use, property described in paragraph (2) of Article 14 in such State shall be treated as income from sources within such State.

4. Income from real property (including gains derived from the sale of such property, but not including interest from mortgages or bonds secured by real property) and royalties from the operation of mines, quarries, or other natural resources shall be treated as income from sources within the State in which such property is located.

5. Income from the rental of tangible personal (movable) property shall be treated as income from sources within the country in which such property is located.

6. Income received by an individual for his performance of personal services (either as an employee or in an independent capacity) or for furnishing the personal services of another person and income received by a corporation for furnishing the personal services of its employees or others shall be treated as income from sources within the State in which such services are performed. If services are performed partly within and partly outside a State, income from the performance or furnishing of such services shall be treated as income from sources partly within and partly outside that State. Compensation for personal services (including private pensions and annuities paid in respect of such services) performed aboard ships or aircraft operated by a resident or corporation of a Contracting State and registered in that Contracting State shall be treated as income from sources within that Contracting State, if rendered by a member of the regular complement of the ship or aircraft.

7. Income from the purchase and sale of personal (movable) property shall be treated as income from sources within the State in

which such property is sold.

8. In the case of income earned by a person from the sale of personal property produced in whole or in part by such person in one State and sold in another State, that portion of the income attributable to production shall be treated as income from sources in the State in which such property was produced while that portion attributable to the act of sale shall be treated as income from sources in the State in which such property was sold.

9. Industrial and commercial profits which are attributable to a permanent establishment situated in one of the Contracting States, including income dealt with in Articles 12, 13, 14 or 15 which is effectively connected with such permanent establishment, shall be treated as income from sources within such Contracting State. For the purposes of this Convention, to determine whether income is effectively connected with a permanent establishment, the factors taken into account shall include whether the income is derived from assets used in or held for use in the conduct of such trade or business, or the activities of such trade or business were a material factor in the realization of the income. In determining whether an asset is used in or held for use in the conduct of such trade or business or whether the activities of such trade or business were a material factor in realizing an item of income, due regard shall be given to whether or not such asset or such income was accounted for through such trade or business.

10. The source of any item of income to which the provisions of this Article are not expressly applicable shall be determined by each of the Contracting States in accordance with its own law.

Article 6

Nondiscrimination

1. A national of one of the Contracting States who is a resident of the other Contracting State shall not be subjected in that other Contracting State to more burdensome taxes than is a national of that other Contracting State who is resident therein.

2. A permanent etablishment which a national or corporation of one of the Contracting States has in the other Contracting State shall not be subject in that other Contracting State to more burdensome taxes than is a national or corporation of that other Contracting State carrying on the same activities. This paragraph shall not be construed as obliging either Contracting State to grant to nationals of the other Contracting State who are not residents of the former Contracting State any personal allowances or deductions which are by its law available only to residents of that former Contracting State.

3. A corporation of one of the Contracting States, the capital of which is wholly or partly owned by one or more nationals or corporations of the other Contracting State, shall not be subjected in the former Contracting State to more burdensome taxes than is a corporation of the former Contracting State, the capital of which is wholly owned by one or more nationals or corporations of that former Contracting State.

Article 7

Investment Credit

1. The United States shall allow to an eligible investor in an eligible corporation against the taxes specified in subparagraph (1) (b) of Article 1, a credit for investment in Brazil. The credit allowed to an eligible investor shall be based on 7 percent of the appropriate amount of the qualified property

placed in service by the eligible corporation during such corporation's taxable year, for use exclusively in Brazil in a qualified trade or business. The purpose of this provision is to extend to investment in Brazil the investment credit allowable for investment in the United States. Qualified property shall include, in general, tangible depreciable property which is either personal property or is used as an integral part of industrial, transportation, communication or other such similar processes, or as a research or storage facility therefor (but not including a building and its structural components). However, in no event shall the amount of the credit exceed the lesser of—

a) 7 percent of the eligible investor's net new investment in the eligible corporation; or

b) the amount of United States property acquired by the eligible corporation, during its taxable year in which it placed in service the property for which a credit is allowed, or during the preceding taxable year, and attributed to the eligible investor.

2. In determining an eligible investor's net new investment in an eligible corporation, there shall be taken into account—

a) any property transferred by the eligible investor to the eligible corporation as a cóntribution to capital or in exchange for stock or indebtedness of the eligible corporation, but only to the extent that such property does not represent, directly or indirectly, funds borrowed within Brazil;

b) the eligible investor's allocable share of creditable reinvested earnings of the eligible corporation;

c) an appropriate amount with respect to the exhaustion of property placed in service by the eligible corporation for which a credit had previously been allowed under this Article;

d) the amount of property withdrawn by the eligible investor from the eligible corporation in the taxable year, the preceding taxable year, and the three subsequent taxable years.

3. For purposes of this Article—

a) the term "eligible investor" means a recorporation which owns, or is a member of a group of United states residents or corporations which owns, at least 25 percent of the total combined voting power of the stock of an eligible corporation.

b) the term "eligible corporation" means a United States corporation or a Brazilian corporation if, for its taxable year, it derives at least 80 percent of its gross income, if any, from, and at least 80 percent of its assets (including assets located outside Brazil) are used or held for use in connection with, one or more of the qualified trades or businesses described in subparagraph (c).

c) the term "qualified trade or business" means, unless otherwise agreed by the competent authorities of the Contracting States, any trade or business conducted within Brazil, and consisting of:

(i) the manufacture or production of personal property (not including the extraction of any mineral, ore, oil or gas, or any processing which does not involve a substantial transformation thereof, but not excluding smelting or refining) or the processing of agricultural or horticultural products or commodities (including but not limited to livestock, poultry, fur-bearing animals or any kind of fish);

(ii) the catching or taking of any kind of fish;

(iii) the marketing of agricultural or horticultural products or commodities (including but not limited to livestock, poultry, fur-bearing animals or any kind of fish);

(iv) the marketing of goods and merchandise to the general public through one or more retail establishments, unless the business consists primarily of the distribu-

tion of goods or merchandise manufactured or produced outside. Brazil by a person who is a related person with respect to the eligible corporation;
(v) the operation of hotels and related facilities;
(vi) the transportation within Brazil of passengers and/or freight;
(vii) the performance of services rendered as an incident of a trade or business described in (i) through (vi); or
(viii) the performance within Brazil of services utilized either within Brazil or within a less developed country if the services are industrial, financial, technical, scientific, engineering or architectural in nature. The preceding sentence shall not apply if the services are performed for any person who is a related person with respect to the eligible corporation and if the payments made in consideration of such services are not reasonable in amount or are contingent either in whole or in part on the sales, productivity, or profits of the person for whom these services are performed; and
(ix) any other trade or business agreed upon by the competent authorities of both Contracting States.

d) the term "creditable reinvested earnings" means an amount equal to one-half of the earnings and profits of the eligible corporation for its taxable year, reduced by the amount of any dividends it distributed during such year.

e) the term "withdrawal" means—
(i) a distribution made by an eligible corporation (or by another corporation conducting in Brazil a trade or business similar or related to a trade or business conducted by the eligible corporation) to the eligible investor (or to a related person) which either—
(A) is not out of earnings and profits;
(B) is in excess of 50 percent of the earnings and profits for the year of distribution; or
(C) is in cancellation or redemption of the stock of the eligible corporation;
(ii) the payment by an eligible corporation of an indebtedness to the eligible investor; and
(iii) the sale or other disposition by the eligible investor of stock or indebtedness of the eligible corporation.

f) the term "United States property" means any tangible property which has been manufactured, constructed, produced, grown, extracted or created in the United States and thereafter continuously used, if at all, only in the United States.

4. a) If the credit allowed for investment in the United States is modified, amended, suspended or terminated, the comparable provisions of this Article shall accordingly be modified, amended, suspended or terminated to the extent necessary to keep this Article consistent with the credit allowed for investment in the United States. The United States shall notify Brazil through diplomatic channels of any such modification, amendment, suspension or termination.

b) If Brazil considers that any modification or amendment of the credit, as a result of subparagraph (a), materially and adversely affects the credit allowed under this Article, it may, by giving notice to the United States through diplomatic channels, treat such modification or amendment as a suspension of the credit for purposes of subparagraph (6) (b) of Article 30. In such case the Contracting States shall consult together. At any time prior to such consultation, and until such time as a supplementary agreement is reached by the Contracting States, the United States may, by notice given to Brazil through diplomatic channels, suspend the application of Article 7.

5. The credit provided in paragraph (1) shall be subject to such regulations as are prescribed by the Secretary of the Treasury of the United States or his delegate, after consultation with the competent authority of Brazil, to effectuate the provisions of this Article and to further define and determine the terms, conditions and amounts referred to herein.

Article 8

Business Profits

1. A resident or corporation of one of the Contracting States shall be exempt from tax in the other Contracting State with respect to its industrial or commercial profits if that resident or corporation has no permanent establishment in that other Contracting State. If a resident or corporation of one of the Contracting States has a permanent establishment in the other Contracting State, tax may be imposed by such other Contracting State on all industrial or commercial profits of that resident or corporation which are (a) attributable to the permanent establishment or (b) derived from sources within such other State from sales of goods or merchandise of the same kind as those sold, or from other business transactions of the same kind as those effected, through the permanent establishment.

2. For purposes of paragraph (1) (a) of this Article, there shall in each Contracting State be attributed to a permanent establishment the industrial or commercial profits which would be attributable to such permanent establishment if such permanent establishment were an independent entity engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the resident of which it is a permanent establishment.

3. In determining the industrial or commercial profits of an enterprise of one of the Contracting States which are taxable in the territory of the other Contracting State in accordance with paragraphs (1) and (2), there shall be allowed as deductions all expenses (including executive and general administrative expenses) which would be deductible if the permanent establishment were an independent enterprise and which are reasonably connected with the profits so taxable.

4. No profits shall be deemed to be derived merely by reason of the purchase of goods or merchandise by that permanent establishment, or by the resident or corporation of which it is a permanent establishment, for the account of that resident or corporation.

5. The term "industrial or commercial profits" means income derived from the active conduct of a trade or business. It includes profits from manufacturing, mercantile, agricultural, fishing, from transportation, communication or extractive activities, from the rental of tangible personal (movable) property, from the furnishing by an individual of the personal services of another person and from the furnishing by a corporation of the personal services of its employees, or others. It also includes income dealt with in Article 12 (dividends and profits), Article 13 (interest), Article 14 (royalties), or Article 15 (real property and natural resource income), but only if the right or property giving rise to such income is effectively connected with a permanent establishment which the recipient, being a resident or corporation of one Contracting State, has in the other Contracting State. It does not include income received by an individual for his performance of personal services (either as an employee or in an independent capacity).

Article 9

Definition of Permanent Establishment

1. The term "permanent establishment" means a fixed place of business through which a resident or corporation of one of the Contracting States engages in trade or business.
2. The term "a fixed place of business" includes, but is not limited to, an office; a store or other sales outlet; a workshop; a factory; a warehouse; a mine, quarry or other place of extraction of natural resources; a building, construction or installation site.
3. Notwithstanding paragraph (1) of this Article, a permanent establishment shall not include a fixed place of business used only for one or more of the following activities:
a) for the processing by another person, whether related or unrelated, under arrangements or conditions which are or would be made between independent persons, of goods or merchandise belonging to the resident or corporation;
b) for the purchase, under arrangements or conditions which are or would be made between independent persons, of goods or merchandise for the account of the resident or corporation;
c) for the storage and/or delivery of goods belonging to the resident or corporation, other than goods or merchandise:
(i) held for sale by such resident or corporation in a store or other sales outlet; or
(ii) purchased and resold in that Contracting State by the resident or corporation, or by an independent agent or agents for or on behalf of the resident or corporation;
d) for the collection of information for the resident or corporation;
e) for advertising, the conduct of scientific research, the display of goods or merchandise, or the supply of information if such activities have a preparatory and auxiliary character in the trade or business of the resident or corporation;
f) for construction, assembly, or installation projects if the site or facilities are used for such purpose for less than six months.
4. Even if a resident or corporation of one of the Contracting States does not have a permanent establishment in the other Contracting State under paragraphs (1)-(3) of this Article, nevertheless he shall be deemed to have a permanent establishment in the latter State if he engages in trade or business in that State through an agent who—
a) has an authority to conclude contracts in the name of that resident or corporation and regularly exercises that authority in the latter State unless the exercise of his authority is limited to the purchase of goods or merchandise; or
b) maintains in the latter State a stock of goods or merchandise belonging to that resident or corporation from which he regularly makes deliveries.
5. Notwithstanding paragraph (4) of this Article, a resident or corporation of a Contracting State shall not be deemed to have a permanent establishment in the other Contracting State merely because it uses the services in that State of a bona fide broker, general commission agent, forwarding agent, custodian or other agent of independent status acting in the ordinary course of his business.
6. The fact that a corporation of one of the Contracting States controls or is controlled by or is under common control with (a) a corporation of the other Contracting State or (b) a corporation which engages in trade or business in that Contracting State (whether through a permanent establishment or otherwise), shall not be taken into account in determining whether the activities or fixed place of business of either corporation con-

stitutes a permanent establishment of the other corporation.

7. A resident or corporation of one of the Contracting States shall be deemed to have a permanent establishment in the other Contracting State if that resident or corporation provides the services in the latter State of public entertainers referred to in paragraph (4), Article 17.

8. If a resident or corporation of one of the Contracting States has a permanent establishment in the other Contracting State at any time during the taxable year, it shall be considered to have a permanent establishment in that other Contracting State for the entire taxable year.

Article 10

Ships and Aircraft

1. Notwithstanding paragraph (2) of Article 8, income which a resident or corporation of the United States derives from the operation in international traffic of ships or aircraft registered in the United States shall be exempt from tax by Brazil.

2. Notwithstanding paragraph (2) of Article 8, income which a resident or corporation of Brazil derives from the operation in international traffic of ships or aircraft registered in Brazil shall be exempt from tax by the United States.

Article 11

Related Persons

1. Where a resident or corporation of a State deriving industrial or commercial profits in one of the Contracting States and any other person are related and where such related persons make arrangements or impose conditions between themselves which are different from those which would be made between independent persons, then any income which would, but for those arrangements or conditions, have accrued to such resident or corporation but, by reason of those arrangements or conditions, has not so accrued, may be included in the income of such resident or corporation for purposes of the present Convention and taxed by that Contracting State accordingly.

2. a) A person other than a corporation is related to a corporation if such person participates directly or indirectly, in the management, control or capital of the corporation.

b) A corporation is related to another corporation if either participates directly or indirectly in the management, control or capital of the other, or if any person or persons participate directly or indirectly in the management, control or capital of both corporations.

Article 12

Dividends and Branch Profits

1. Dividends paid by a company resident in one of the Contracting States to a resident or corporation of the other Contracting State may be taxed by both Contracting States.

2. For purposes of this Article:

a) In the case of Brazil, the term "dividends" means income from shares, "jouissance" shares or "jouissance" rights, mining shares, founders' shares or other rights, not being debt-claims, participating in profits, as well as income from other corporate rights assimilated to income from shares, including all other forms of distribution of profits made by any type of company or individual enterprise situated in Brazil.

b) The term "dividends" in the case of the United States includes any item which under the law of the United States is treated as a distribution out of earnings and profits.

3. The rate of the withholding tax imposed by Brazil on dividends paid by a corporation

of Brazil to a corporation of the United States shall not exceed 20 percent, if–

a) During the part of the paying corporation's taxable year which precedes the date of payment of the dividend and during the whole of its prior taxable year (if any) at least 10 percent of the outstanding shares of the voting stock of the paying corporation was owned by the recipient corporation, and

b) Not more than 25 percent of the gross income of the paying corporation for such prior taxable year (if any) consisted of interest and dividends (other than interest derived in the conduct of a banking, insurance or financing business and dividends or interest received from subsidiary corporations, 50 percent or more of the outstanding shares of the voting stock of which was owned by the paying corporation at the time such dividends or interest were received).

4. The rate of the withholding tax imposed by Brazil on profits of a Brazilian branch of a United States corporation shall not exceed the rate described in paragraph (3).

5. Notwithstanding the provisions of paragraphs (3) and (4) of this Article, the rate of withholding tax on dividends and on branch profits may be increased to the same extent as any reduction below 28 percent in the rate of tax on business profits normally applicable to all industrial or commercial profits of corporations in Brazil.

6. Dividends paid by a corporation of one of the Contracting States to a person other than a resident or corporation of the other Contracting State (and in the case of a dividend paid by a Brazilian corporation, to a person other than a citizen of the United States) shall be exempt from tax by the other Contracting State. This paragraph shall not apply if–

a) Such dividends are treated as income from sources within that other Contracting State under subparagraph (1) (b) of Article 5, or

b) The recipient of the dividends has a permanent establishment in the other Contracting State and such dividends are effectively connected with such permanent establishment.

Article 13

Interest

1. Interest derived from sources within one of the Contracting States by a resident or corporation of the other Contracting State may be taxed by both Contracting States.

2. Interest received by the Government of one of the Contracting States or any agency or instrumentality wholly owned by that Government shall be exempt from tax by the other Contracting State.

3. The tax imposed by Brazil on interest received from sources within Brazil by a resident or corporation of the United States which is a bank or other financial institution shall not exceed 15 percent of the amount paid. This paragraph shall not apply if the recipient of such interest has a permanent establishment in Brazil. In such case, such interest shall be treated as industrial or commercial profits attributable to such permanent establishment and the provisions of Article 8 shall apply thereto.

4. The term "interest" as used in this Article means income from Government securities, bonds or debentures, whether or not secured by mortgage and whether or not carrying a right to participate in profits, and debt-claims of every kind as wel as all other income assimilated to income from money lent by the taxation law of the State in which the income arises.

5. Where, owing to a special relationship between the payer and the recipient or between both of them and some other person, the amount of the interest paid, having regard to the debt-claim for which it is paid,

exceeds the amount which would have been agreed upon by the payer and the recipient in the absence of such relationship, the provisions of paragraph (3) of this Article shall apply only to the last-mentioned amount. In that case, the excess part of the payments shall remain taxable according to the law of each Contracting State, due regard being had to the other provisions of this Convention.

6. Interest paid by a corporation of one of the Contracting States to a person other than a resident or corporation of the other Contracting State (and, in the case of interest paid by a Brazilian corporation, other than a citizen of the United States) shall be exempt from tax by the other Contracting State. This paragraph shall not apply if—

a) such interest is treated as income from sources within that other Contracting State under subparagraph (2) (b) of Article 5, or

b) the recipient of the interest has a permanent establishment in the other Contracting State and such interest is effectively connected with such permanent establishment.

Article 14

Royalties

1. The tax imposed by one of the Contracting States on royalties derived from sources within that Contracting State by a resident or corporation of the other Contracting State shall not exceed 15 percent of the gross amount thereof. This paragraph shall not apply if the recipient of such royalties has a permanent establishment in the other Contracting State. In such case, such royalties shall be treated as industrial or commercial profits attributable to such permanent establishment and the provisions of Article 8 shall apply thereto.

2. For the purpose of paragraph (1) of this Article, the term "royalties" means any royalties, rentals or other amounts paid as consideration for the use of, or the right to use—

a) copyrights, artistic or scientific works, patents, designs, plans, secret processes or formulae, or other like property or rights;

b) information concerning industrial or scientific knowledge, experience, or skill; or

c) trademarks related to any of the items specified in subparagraph (a) or (b).

3. The provisions of paragraphs (1) and (2) of this Article shall not apply to any royalties, rentals or other amounts paid:

a) in respect of the operation of mines, quarries or other natural resources;

and

b) as consideration for the use of, or the right to use, motion picture films, films or tapes for radio, television broadcasting, or other like property or rights.

4. Where any royalty exceeds a fair and reasonable consideration in respect of the rights for which it is paid, the provisions of the present Article shall apply only to so much of the royalty as represents such fair and reasonable consideration in accordance with the provisions of the tax legislation of the Contracting State from which the royalty is derived. Where, owing to a special relationship between the payer and the recipient or between both of them and some other person, the amount of the royalties paid, having regard to the use, right or information for which they are paid, exceeds the amount which would have been agreed upon by the payer and the recipient in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In both cases, the excess part of the payments shall remain taxable according to the law of each Contracting State, due regard being had to the other provisions of this Convention.

Article 15

Income from Real Property

A resident or corporation of one of the Contracting States subject to tax in the other Contracting State on income from real property, including gains derived from the sale or exchange of such property, or on royalties, in respect of the operation of mines, quarries, or other natural resources, may elect for any taxable year to compute that tax on such income on a net basis as if such resident or corporation were engaged in trade or business in that other Contracting State.

Article 16

Investment or Holding Companies

A corporation of one of the Contracting States deriving dividends, interest or royalties from sources within the other Contracting State shall not be entitled to the benefits of Article 12, Article 13, or Article 14 if (a) by reason of special measures granting tax benefits to investment or holding companies the tax imposed on such corporation by the former Contracting State with respect to such dividends, interest or royalties is substantially less than the tax generally imposed by such Contracting State on corporate profits, and (b) 25 percent or more of the capital of such corporation is held of record or is otherwise determined, after consultation between the competent authorities of the Contracting States, to be owned, directly or indirectly, by one or more persons who are not individual residents of the former Contracting State (or, if residents of Brazil, are citizens of the United States).

Article 17

Income from Personal Services

1. An individual who is a resident of one of the Contracting States shall be exempt from tax by the other Contracting State with respect to income from personal services if—
a) he is present within the latter Contracting State for a period or periods not exceeding in the aggregate 183 days during the taxable year; and either
b) in the case of employment income—
(i) such individual is an employee of a resident or corporation of a State other than the latter Contracting State (or of a permanent establishment of a resident or corporation of the latter Contracting State located outside the latter Contracting State); and
(ii) such income is not deducted as such in computing the profits of a permanent establishment in the latter Contracting State which are subject to tax in that State; or
c) such income does not exceed $4,000 or its equivalent in Brazilian cruzeiros.
2. Compensation received by any individual for personal services performed aboard ships or aircraft operated by a resident or corporation of a Contracting State and registered in such Contracting State shall, subject to paragraph (3) of Article 3, be exempt from tax by the other Contracting State, if the services are rendered by a member of the regular complement of the ship or aircraft.
3. For purposes of paragraph (1), the term "income from personal services" includes employment income and income earned by an individual from the performance of personal services in an independent capacity. The term "employment income" includes income from services performed by officers and directors of corporations, but does not include income from personal services performed by partners, which shall be treated as income from the performance of services in an independent capacity.
4. Income derived by a public entertainer, theatre, motion picture or television artist,

musician or athlete from his personal activities as such, even though otherwise exempt under paragraph (1) of this Article, shall not be exempt if such income exceeds $100 or its equivalent in Brazilian cruzeiros, for each day such person is present in the other Contracting State.

Article 18

Teachers

1. An individual who is a resident of one of the Contracting States at the beginning of his visit to the other Contracting State and who, at the invitation of the Government of the other Contracting State or of a university or other accredited educational institution situated in the other Contracting State, visits the latter Contracting State for the primary purpose of teaching or engaging in research, or both, at a university or other accredited educational institution shall be exempt from tax by the latter Contracting State on his income from personal services for teaching or research at such educational institution, or at other such institutions, for a period not exceeding two years from the date of his arrival in the latter Contracting State.

2. This Article shall not apply to income from research if such research is undertaken not in the public interest but primarily for the private benefit of a specific person or persons.

Article 19

Students and Trainees

1. a) An individual who is a resident of one of the Contracting States at the beginning of his visit to the other Contracting State and who is temporarily present in the other Contracting State for the primary purpose of—

(i) studying at a university or other accredited educational institution in that other Contracting State;

(ii) securing training required to qualify him to practice a profession or a professional specialty; or

(iii) studying or doing research as a recipient of a grant, allowance, or award from a governmental, religious, charitable, scientific, literary or educational organization,

shall be exempt from tax by that other Contracting State with respect to—

(A) gifts from abroad for the purposes of his maintenance, education, study, research or training;

(B) the grant, allowance, award; and

(C) income from personal services performed in the other Contracting State in an amount not in excess of $2,000 or its equivalent in Brazilian cruzeiros for any taxable year; or, of such individual is securing training required to qualify him to practice a profession or a professional specialty, not in excess of $5,000 or its equivalent in Brazilian cruzeiros for any taxable year.

b) The benefits under this paragraph shall only extend for such period of time as may be reasonably or customarily required to effectuate the purpose of the visit, but in no event shall any individual have the benefits of this paragraph for more than five taxable years.

2. A resident of one of the Contracting States who is present in the other Contracting State for a period not exceeding one year, as an employee of, or under contract with, a resident or corporation of the former State, for the primary purpose of—

(i) acquiring technical, professional, or business experience from a person other than that resident or corporation of the former State or a corporation 50 percent or more of the voting stock of which is owned by that corporation of the former State; or

(ii) studying at a university or other accredited educational institution in that other Contracting State;

shall be exempt from tax by that other Contracting State with respect to his income from personal services performed in the other Contracting State for that period in an amount not in excess of $5,000 or its equivalent in Brazilian cruzeiros.

3. A resident of one of the Contracting States who is present in the other Contracting State for a period not exceeding one year, as a participant in a program sponsored by the Government of the other Contracting State, for the primary purpose of training, research or study, shall be exempt from tax by that other State with respect to his income from personal services performed in that other Contracting State and received in respect of such training, research, or study in an amount not in excess of $10,000 or its equivalent in Brazilian cruzeiros.

Article 20

Governmental Salaries

Wages, salaries, and similar compensation, and pensions, annuities, or similar benefits paid by, or from public funds of, one of the Contracting States or the political subdivisions thereof to an individual who is a national of that Contracting State for services rendered to that Contracting State or to any of its political subdivisions in the discharge of governmental functions shall be exempt from tax by the other Contracting State.

Article 21

Rules Applicable to Personal Income Articles

1. Articles 17, 18, 19 and 20 shall apply to reimbursed travel expenses, but such expenses shall not be taken into account in computing the maximum amount of exemptions specified in Articles 17 and 19.

2. An individual who qualifies for benefits under more than one of the provisions of Articles 17, 18, 19 and 20 may apply that provision most favorable to him, but he shall not be entitled to the benefits of more than one provision in any taxable year.

Article 22

Deduction for Charitable Contributions

In the computation of taxable income under the United States income tax, a deduction shall be allowed to citizens and residents of the United States and to United States corporations for contributions to any organization created or organized under the laws of Brazil which constitutes a nonprofit organization exempt from tax for purposes of the income tax laws of Brazil if—

a) such contributions are used entirely within Brazil and

b) the recipient organization has qualified as an exempt organization under subsection 501 (c) (3) of the United States Internal Revenue Code.

Such deduction shall not exceed an amount which would be allowable under the United States Internal Revenue Code if such organization were created or organized under the laws of the United States and if such contributions were used within the United States.

Article 23

Pensions and Annuities

1. Private pensions and private life annuities paid to individuals who are residents of one of the Contracting States shall be exempt from tax by the other Contracting State.

2. The term "life annuities", as used in this Article, means a stated sum paid periodically

at stated times during life, or during a specified number of years, under an obligation to make the payments in return for adequate and full consideration.

3. The term "pensions", as used in this Article, means periodic payments made after retirement or death in consideration for, or by way of compensation for injuries received in connection with, past employment.

Article 24

Consultation

1. The competent authorities of the Contracting States may communicate with each other directly for the purpose of giving effect to the provisions of the present Convention. Should any difficulty or doubt arise as to the interpretation or application of the present Convention, or its relationship to conventions between one of the Contracting States and any other State, the competent authorities shall endeavour to settle the question as quickly as possible by mutual agreement.

2. In particular, the competent authorities of the Contracting States may consult together to endeavour to agree—

a) to the same application of the source rules set forth in Article 5 to particular items of income;

b) to the same attribution of industrial or commercial profits to a resident or corporation of one of the Contracting States and to its permanent establishment situated in the other Contracting State; or

c) to the same allocation of income between a resident or corporation of one of the Contracting States and any related person, provided for in Article 11.

In the event that the competent authorities reach such an agreement, taxes shall be imposed on such income and refund or credit of taxes shall be allowed by the Contracting States in accordance with such agreement.

Article 25

Exchange of Information

1. The competent authority of one of the Contracting States shall exchange such information with the competent authority of the other Contracting State as is pertinent to carrying out the provisions of the present Convention or preventing fraud or fiscal evasion in relation to the taxes which are the subject of the present Convention.

2. The competent authority of the Contracting State to which a request for information is made shall not exchange information unless that information would be available under the taxation laws and administrative procedures of that State if the tax of the other State, to which the request for information relates, were the tax of the former State and were being imposed by that State.

3. Any information exchanged shall be treated as secret but many be disclosed to persons (including a court or administrative body) concerned with assessment, collection, enforcement or prosecution with respect to the taxes which are the subject of the present Convention.

4. No information shall be exchanged which would disclose any trade, business, industrial, or professional secret.

Article 26

Assistance in Collection

1. Each of the Contracting States shall endeavour to collect such taxes imposed by the other Contracting State as will ensure that any exemption or reduced rate of tax granted under the present Convention by the other State shall not be enjoyed by persons not entitled to such benefits. The Contracting State making such collections shall be responsible to the other Contracting State for the sums thus collected. The competent au-

thority of each of the Contracting States shall consult with the competent authority of the other Contracting State for the purpose of cooperating with and advising that other Contracting State in respect of any action taken by it within the former Contracting State to collect its tax.

2. In no case shall the provisions of this Article be construed so as to impose upon either of the Contracting States the obligation to carry out administrative measures at variance with the regulations and practices of the Contracting State endeavouring to collect the tax or which would be contrary to that State's sovereignty, security or public policy.

Article 27

Taxpayer Claims

A taxpayer shall be entitled to present his case to the Contracting State of which he is citizen or resident, or, if the taxpayer is a corporation of one of the Contracting States, to that State, if he considers that the action of the other Contracting State has resulted, or will result for him in taxation contrary to the provisions of this Convention. Should the taxpayer's claim be considered to have merit by the competent authority of the Contracting State to which the claim is made, it shall endeavor to come to an agreement with the competent authority of the other Contracting State with a view to the avoidance of taxation contrary to the provisions of the Convention.

Article 28

Exchange of Legal Information

1. The competent authorities of the Contracting States shall notify each other of any amendments of the tax laws referred to in Article 1 (1) and of the adoption of any taxes referred to in Article 1 (2) by transmitting the text, of any amendments or new statutes at least once a year.

2. The competent authorities of the Contracting States shall exchange the texts of all published material interpreting the present Convention under the laws of the respective States, whether in the form of regulations, rulings or judicial decisions.

3. For the purpose of mutual assistance in the development and maintenance of sound fiscal policies and tax administration, the competent authorities of the Contracting States may on the initiative of either, consult together and make such arrangements as may be mutually acceptable, including exchanges of personnel and of technical memoranda and studies.

4. The texts transmitted under this Article shall be in the language of the transmitting State.

Article 29

Diplomatic and Consular Officers

The provisions of the Convention shall not prejudice the tax privileges enjoyed by diplomatic or consular offices by virtue of general rules of international law or the provisions of special agreements.

Article 30

Effective Dates and Ratification

1. The present Convention shall be ratified and the instruments of ratification exchanged at Washington as soon as possible.

2. After the exchange of instruments of ratification, the present Convention shall have effect for taxable years beginning on or after the first day of January of the year following the exchange of instruments of ratification.

3. Notwithstanding the provisions of paragraph (2) of this Article—

a) Paragraph (8) of Article 5 shall have effect only after the competent authorities of both Contracting States have established mutually acceptable rules for implementation of such paragraph.
b) Article 7 shall have effect with respect to property placed in service and net new investments made on or after January 1, 1968.
c) Articles 12, 13 and 14 shall have effect with respect to amounts paid on or after January 1, 1969.
4. The present Convention shall continue in effect indefinitely, but it may be terminated by either of the Contracting States, at any time after three years from the first day of January referred to in paragraph (2) of this Article, provided that at least six months' prior notice of termination has been given through diplomatic channels. In such event, the present Convention shall cease to be effective for taxable years beginning on or after the first day of January next following the expiration of the six-months period.
5. Notwithstanding the provisions of paragraph (4) of this Article and upon six months' prior notice to be given through diplomatic channels—
a) paragraph (8) of Article 5, and any rules established for the implementation of such paragraph by agreement of the competent authorities of both Contracting States, may be terminated by either Contracting State at any time.
b) the benefits provided under Articles 7 or 22 may be terminated by the United States at any time after three years from the date specified in paragraph (2) of this Article.
c) the provisions of paragraphs (3) and (4) of Article 12, paragraph (3) of Article 13, and paragraph (1) of Article 14 may be terminated by Brazil at any time after three years from the date specified in paragraph (2) of this Article.
6. Notwithstanding the provisions of paragraphs (4) and (5) of this Article, the provisions of paragraphs (3) and (4) of Article 12, paragraph (3) of Article 13, and paragraph (1) of Article 14 may, by notice given by Brazil to the United States through diplomatic channels, be—
a) terminated by Brazil at any time after the date on which the credit provided by Article 7 is terminated pursuant to paragraph (4) thereof; or
b) suspended by Brazil at any time after the date, and for the period, of any suspension of the credit provided by Article 7 pursuant to paragraph (4) thereof.
7. Any termination or suspension under paragraphs (5) or (6) shall not prejucide benefits available with respect to transactions entered into prior to such termination.
In WITNESS WHEREOF, the undersigned Plenipotentiaries have signed the present Convention.
Done at Rio de Janeiro, in duplicate, in the English and Portuguese languages, both texts authentic, this 13th day of March on thousand nine hundred and sixty seven.

For the Government of the United States of America:
(SEAL)
JOHN TUTHILL

For the Government of the United States of BRAZIL:
(SEAL)
JURACY MAGALHAES
OCTAVIO BULHOES

Rhodesia: Report of the Committee on the Value Added Turnover Taxation

SUPPLEMENT TO THE BULLETIN FOR INTERNATIONAL FISCAL DOCUMENTATION
AU BULLETIN DE DOCUMENTATION FISCALE INTERNATIONALE

Vol XXI, No. 12, December/décembre 1967

INTERNATIONAL BUREAU OF FISCAL DOCUMENTATION

Muiderpoort - 124 Sarphatistraat - Amsterdam

In August 1966 a Committee was appointed by the Rhodesian Minister of Finance with the following terms of reference: "To report on the advantages and disadvantages of introducing a form of value added turnover tax. In considering this matter, the Committee should have regard to

1) encouraging the rapid development of the economy by means of incentives to increased production and the promotion of exports;
2) ensuring a fair distribution of the burden of taxation including taxation within the income tax field;
3) maintaining revenue yields;
4) achieving maximum efficiency and simplicity in tax collection."

The Committee submitted its report in June 1967.

This Supplement contains the Committee Report in full, excluding however an appendix concerning a "Possible Phasing Programma", this being of less international interest. It should be noted that the abbrevation VAT in the text of the Report is used to refer to the value added.

TEXT

CHAPTER I

WHAT IS VALUE ADDED TAX?

1. Although the Committee was asked to consider the value added turnover tax only, it was decided at the outset that it was important to a proper appreciation of this tax to set it in relief against a background of other turnover taxes. This chapter, therefore, gives brief descriptions of two or three, followed by a more detailed examination of VAT.

THE RHODESIAN SALES TAX

2. The Rhodesian sales tax is an "add-on" tax applied at a uniform rate of 3⅓ per cent. on retail sales. Because retail prices are ordinarily higher than those charged at earlier stages, a relatively low rate of tax produces the same total revenue as a higher rate imposed at the wholesale or manufacturing stages. For a given total tax yield, a tax imposed at one or more earlier stages than the retail stage could lead to the inflation of profits, and thus retail prices, by the application of successive mark-ups to the tax as well as to the basic price. With the tax at the final stage, not only is a relatively low rate of tax possible, but since only one level of trade is affected, the danger of price inflation is minimized.

3. Under the Rhodesian legislation a registered operator may purchase goods intended for resale from another registered operator without payment of tax. In addition the industrialist is afforded a degree of relief in respect of his purchases in that goods which are to be physically incorporated in the finished product, as well as catalysts, chemical processing agents and some fuels, are not subject to the tax. The industrialist's other purchases attract tax, however, and therefore his manufacturing costs contain an element of tax from which there is no relief, even in respect of that portion of his output which is exported.

4. Initially certain basic exemptions were allowed but for various reasons the range has subsequently been extended. The widening of the range of exemptions has created administrative difficulties and anomalies which have given rise to major criticisms of the tax. The exclusion of services has also caused anomalies: so has the procedure whereby registration and liability for payment of tax is tied to licensing legislation. Exemptions fall into two basic groups, those dealing with certain input items of industries and a short list of basic food-stuffs, namely bread, maize-meal, uncooked meat and fish, milk and sugar. Export sales are exempt and a countervailing tax is charged on imports. Some capital expenditure is relieved of tax by a system of refunds, but the capital goods in respect of which refunds may be claimed are strictly limited. The "add-on" nature of the tax, which has necessitated the prescribing of the amounts which are to be added to the purchase price, has also given rise to criticism.

CASCADE TAX

5. Under a multi-stage cascade tax each trader is liable quite simply to tax on the whole of his turnover, and there are none of the problems associated with deductions or tax-exempt rings. The system is, therefore, relatively simple to administer.

6. There is, however, one major disadvantage to this form of tax: whereas some goods pass through few stages from producers to consumers, others may pass through many stages and thus attract a greater amount of tax.

7. There may be two main effects. First, an attempt by middlemen to switch wherever possible to a commission basis so that their liability to the tax is minimized; this may create inequities for those trading organizations which are not suited to operation on a commission basis. Second, the encouragement of vertical integration whereby one firm controls the entire process of production and distribution from manufacturing to retailing; this is not necessarily desirable and in any event there are some industries which are unsuitable for, or incapable of, vertical integration.

8. One advantage of the cascade system is that it makes possible a very low rate of tax, which is more acceptable by the public. Against this there is the problem of a cascade

not only in tax but also in profits where mark-ups are based on tax inclusive prices. Another difficulty is that of determining the correct amount of tax to be remitted on exports and the proper rate to be charged on imports.

9. The cascade tax is tending to be replaced with value added tax. Western Germany is one country where this is happening at the present time.

VALUE ADDED TAX

10. "Value added" has been defined in broad terms as the difference between income from sales and expenditure on the purchase of goods and services from others. It thus corresponds with the total amount spent on wages, salaries, interest and similar outlays, plus profit*, and the aim of the value added tax is to strike not the entire sales price but only those elements of the price which comprise "value added".

11. Since France is usually regarded as the pioneer in the field of VAT it may be useful at this point to trace briefly the history of the development of turnover taxes there. Until 1948, France imposed in succession a cascade tax, a specialized single stage tax, and finally a tax imposed at the production stage. Under the production tax, taxable goods were transferable from one producer to another without payment of tax if the goods were to undergo a further process of manufacture. For other goods this meant that an element of "tax-on-tax" remained. In particular, this tax imposed a heavy burden on investment and thus had some impact on export prices. The subsequent success of the French tax on "value added" in relation to re-eqiupment and exports may be attributed largely to the removal of its predecessors' disincentive effects in these fields.

12. The progress from 1948 to the present tax in France was achieved in two stages. In the first, the system of suspension of tax was abolished and instead a fractional payments system was adopted, so that producers could deduct from their own tax liability the tax included in the cost of their purchases of raw materials. In the second and more important stage, a deduction of tax was allowed on investment goods and on goods consumed in the production process.

13. It will be apparent that "value added" in the context of a turnover tax may have different meanings depending on the extent to which the tax authority wishes to grant relief to taxpayers in respect of their business purchases of goods and services. The Committee felt that it was important to avoid any cascade effect; it also considered that the tax should be rebated on purchases of goods and services of a capital nature. Bearing, these points in mind the Committee was of the opinion that for tax purposes in Rhodesia the most satisfactory definition of "value added" would be the amount by which the value of total turnover from the sale of goods (including sales on capital account) and the provision of services exceeds the value of all purchases of goods and services (including capital purchases) which have already borne tax in the hands of their suppliers. This definition is referred to again, in greater detail, in Chapter VI.

14. The operation of the system may be illustrated by an example in which it is assumed that a tax rate of 10 per cent, applies to both goods and services:—

	£
Total turnover for month (i.e. total of all business sales)	10,000
Less: Selling price of goods exported (these being exempt)	2,000
	8,000

* Note: Hereafter, profit means net profit before taxation, unless the context clearly indicates some other meaning.

Less: Purchases from other taxpayers for business purposes:—		
Trade goods	5,000	
Electricity, water, etc.	100	
Services (e.g. transport, legal expenses, etc.)	200	
Miscellaneous (e.g. stationery)	100	
New motor vehicle	1,000	6,400
Value Added (net taxable amount)		£1,600
Tax is £160, i.e. 10 per cent. of £1,600.		
Check:		
Tax at 10 per cent. on total sales of £10,000		£1,000
Less: Tax rebateable on exports (10 per cent. of £2,000)		200
		800
Less: Tax already paid by suppliers (10 per cent. of £6,400)		640
Net tax payable		£160

15. It must be emphasized that the taxpayer is liable for the full tax on his sales unless he is entitled to deductions in respect of those purchases of goods and services which have already borne tax.

16. Under the rules made in accordance with the General Agreement on Tariffs and Trade, VAT, like other turnover taxes, may be remitted on export sales and parties to the G.A.T.T. are required to take this into account in their customs treatment of imports from other parties who levy turnover taxes.

17. It is of interest to note that following detailed investigations by the European Economic Community into the question of the harmonization of taxes within the common market area, the Council of the Community has chosen the value added system as the model turnover tax and has agreed upon a directive requiring member states to substitute VAT for their existing turnover taxes by 1970.

THE TAX ON SERVICES

18. In many countries the turnover tax is applied not merely to goods but also to services. The inclusion of services within the scope of VAT has obvious attractions. It widens still further the tax base and so ensures an even greater spread of the burden. It also makes possible a lower overall rate of taxation since the same total revenue can be raised by a lower rate from a higher number of transactions. Furthermore it means that suppliers of services may deduct tax paid on goods and services purchased by them.

19. One of the particular problems which arises from a tax on services is how to treat the receipts and accruals of financial institutions, such as banks, acceptance houses and insurance companies. As will be mentioned later in this report the Committee did not examine this problem in detail but merely noted that it would require a separate study.

CHAPTER II

THE HYPOTHETICAL SCHEME

20. At an early stage the Committee realized that its members would need something more tangible to work on than their individual interpretations of the theoretical value added system. Accordingly a hypothetical scheme was devised to give substance to the sort of fiscal reforms which might accompany the introduction of VAT. The scheme proved to be a useful guide and formed a basis for much of the Committee's theorizing on value added tax.

21. Details of the hypothetical scheme are as follows:—

(1) (a) Personal tax to be abolished;
(b) Income tax to be reduced to the following rates:

	Individuals	*Companies*
First £300	1s. 6d. in the £	6s. in the £
Second £300	3s. 0d. in the £	
Third £300	4s. 6d. in the £	
Thereafter	6s. 0d. in the £	

(c) Supertax and undistributed profits tax to be abolished;
(d) The present sales tax to be superseded by a multi-stage value added turnover tax applied right through to and including the retail stage.
(e) A value added tax on services to be introduced.
(f) The tax rate for both goods and services to be 7½ per cent.
(g) Only exports to be exempt.
(h) The tax to be on an "add-in" basis.
(i) Motor fuels to be subject to the tax but the excise to be reduced so as to avoid an increase in price.

(2) (a) It was assumed that wages would rise by no more than the net increased tax burden to consumers; i.e. any price increases resulting from the tax having been passed on in full or in part, less savings on the other taxes.
(b) It was noted that if bread, milk, meat, mealie meal and fish were exempt the tax rate would have to be increased to 8¾ per cent. on the remaining items in order to maintain the total yield in the calculation in the next paragraph.

CHANGE IN TAX BASE

22. It was calculated that the following changes in the tax base would occur:—

A. Increase in Indirect Taxation:	£	£
Estimated net yield from VAT on goods and services		15,700,000
Less: Additional tax on Government purchases	900,000	
Reduction in excise duties on motor fuels	1,300,000	
Sales Tax at 3½ per cent	5,000,000	7,200,000
Net Increase in Indirect Taxation		£8,500,000
B. Decrease in Direct Taxation		£
Income Tax:		
Companies	2,350,000	
Individuals	2,000,000	4,350,000
Supertax		750,000
Undistributed Profits Tax		100,000
Personal Tax		2,400,000
Net Decrease in Direct Taxation		7,600,000
C. Amount available for other concessions		900,000
		£8,500,000

Note: With one exception these calculations have been made on the basis of 1965 transactions, having been derived from the National Accounts for 1965 and the income tax statistics for the year of assessment ended 31st March, 1965. The exception relates to the yield from sales tax where the current rate of 3½ per cent has been used instead of the actual rate of 1⅔ per cent which was effective until June, 1966.

23. An attempt was made to follow these changes through the economy. It is clearly impossible to be precise about the effects at each point but at the risk of some over-simplification of the problems, the Committee is of the opinion that the following represents a fair guide to what might happen:—

(1) Exports. The net return to the exporter after payment of income tax would increase. There would be a lower rate of income tax on profits but there would be no compensating increase in indirect tax either on profits or on costs.

(2) Domestic Market. The amount of profits before payment of income tax would be smaller owing to their having already been subjected to VAT, but the amount of profits remaining after the income tax had been paid would be greater. Furthermore, costs, upon which previously no tax was charged, would now attract VAT and would rise accordingly. The net result would be lower profits unless something were done to correct the situation. One object of VAT is to provide a strong incentive to cut costs through greater efficiency and until this aim

was realized the producer who was unable or unwilling to accept lower profits would have to increase his prices as far as competition would allow. To the extent that he had an export market, he would derive real savings from the tax reforms and these could be applied to his local trading, thereby giving him an advantage over any competitor with a lower export turnover.

(3) Local Consumers. The reductions in direct taxation would benefit the local consumer. The extent of this benefit would vary according to the size of the individual's income: at one end of the scale those in the lower income groups would gain only by the amount of personal tax saved, whilst at the other end those in the high income brackets would gain by the savings in income tax and supertax as well. The consumer would, however, have to bear increases in prices and it is likely that there would be some pressure on wages at the lower levels. In the longer term the consumer could expect to benefit from the effects of increased efficiency and investment.

24. These aspects are discussed in further detail later in this report.

CHAPTER III

THE ADVANTAGES AND DISADVANTAGES OF VAT COMPARED WITH SALES TAX

ADVANTAGES / PREVENTION OF FRAUD AND LOSSES TO THE EXCHEQUER

25. Under the sales tax the main point of collection is at the retail stage and the bulk of the tax is accordingly collected by relatively few firms. Under VAT the tax would be collected from each operator through whose hands a product passed and this system has two main advantages in the context of fraud and losses to the exchequer. First, both parties to a transaction would be directly concerned to ensure that true prices were shown in the documents which recorded the contract. If the seller attempted to avoid tax by rendering an invoice for a lesser amount than was actually payable by the purchaser, his action would, where other things remained equal, operate to the disadvantage of the purchaser whose own added value, and thus his tax liability, would increase. If, on the other hand, the purchaser attempted to avoid tax by requiring an invoice for a larger amount than he had actually paid, the disadvantage would fall upon the seller. The result should be for all operators to pay careful attention to the correctness of the documents reflecting their transactions, particularily since it would be known that a tax inspector might cross-check between the seller's and buyer's records. Second, the potential total amount of tax susceptible to loss would be much smaller in the case of each operator because it would relate solely to his added value and not to the total value of the goods. The incentive and opportunity for tax evasion would be correspondingly reduced.

PAYMENT TO THE EXCHEQUER

26. The sales tax is collected only when the sale to the final consumer takes place, all previous dealings having occurred in the tax-exempt ring. With the value added system of fractional payments the exchequer receives the revenue at a much earlier stage on any particular commodity. Like the PAYE system of income tax collection, therefore, VAT would mean a more regular and constant level of payment to the exchequer.

ENCOURAGEMENT OF EFFICIENCY

27. Finally, there is the question of efficiency. When a manufacturer is directly concerned with the effects of tax on price, especially in the face of competition, a greater urgency is introduced into his search for improved methods. Under the fractional payments system, he would be face to face with the tax aspect, and it would be brought home to him more forcibly that a price reduction carried with it a tax reduction. Competition is itself an incentive, but the tax position is bound to have a greater effect on the producer when he sees it at first hand instead of only at a distance.

DISADVANTAGES/ADMINISTRATION

28. Under the fractional payments system the number of enterprises accounting for the tax would be considerably increased. Furthermore there would be a greater number of clerical processes and a wider field of inspection; and administrative costs would rise, although the Committee does not believe that the rise need be great. Under sales tax the majority of registered operators prior to the retail stage are enabled to buy and sell almost entirely within the exempt ring. The control of this is minimal since a registered operator need only quote his registered number to his supplier for the collection of tax to be suspended. Similarly, he may disregard all tax implications when selling to another registered operator. All registered firms would, under VAT, have to pay tax on their sales and account for it in detail to the state. They would also have to keep proper records of their purchases in order to ensure that tax paid on these was recovered in due course from that payable on sales.

TAX FINANCING

29. Another problem arises out of the need for a registered operator to pay tax-inclusive prices for his purchases. At present, sales tax has almost always been collected in full from the consumer before any payment to the state is made by the trader. There is no doubt that under VAT, where tax is payable in advance of recovery, the overall total of working capital required would be greater. Under sales tax no tax has been paid on stocks but under VAT the tax would already have been paid and a new burden of cost added.

30. Two problems present themselves. First there is the source of capital for this purpose. Concerns with limited resources or limited access to credit might have difficulty in raising the extra capital and could be placed in the position of having to reduce stocks to an unsatisfactory level. Then there is the interest on the extra capital employed: this might be charged to existing profits, or passed on in higher prices.

31. The Committee did not consider that tax financing would be a serious problem. At the date of transition from sales tax to VAT any existing stocks would be tax-exclusive, having already been purchased in the exempt ring. Subsequent purchases would, of course, gradually replace the stock on the shelves until a stage was finally reached where the stock had turned over completely and was all tax-inclusive. However the tax on these purchases would have been deducted month by month and the increased capital requirement would therefore not arise suddenly but would rather accrue in instalments over a lengthy period. This would not be true of a new business being established, when stocks are purchased in bulk at the start, but at least a trader in this position would be aware of the requirement in advance and could arrange his affairs, including his capital, accordingly. The operation of one particular rule in France (known as the "Buffer Rule") aggravates the problem there. Under this rule no refund is made where the deductions

exceed the tax payable on sales: instead a credit is established and must be worked off in future sales. This need not be a feature of VAT and indeed the Committee suggests that monthly accounting, with refunds where necessary, would be preferable from nearly every point of view and would greatly alleviate the problem of tax financing.

SUMMARY

32. The advantages and disadvantages of VAT compared with sales tax may be summarized as follows:—

as to the advantages, VAT—

(a) provides less scope than sales tax for tax evasion and fraud;
(b) accrues to the exchequer at an earlier stage than sales tax and is received by Government on a more evenly distributed basis;
(c) directly affects businessmen at every stage of production and is thus a constant reminder to them of the need for efficiency;

as to the disadvantages, VAT—

(a) involves more administrative processes and higher administrative costs than the sales tax;
(b) might require a higher level of capital investment in stockholdings.

33. On balance the Committee was satisfied that at the rates of tax envisaged in the hypothetical scheme VAT is the superior of the two. Where the rate is very low, however, VAT's incentive to increased efficiency in the productive sectors is so small that it does not outweight the additional administrative costs. As the rate of tax is raised, so the balance of advantage moves in favour of VAT.

34. The Comittee does not believe that the economy would derive any benefit from VAT if it were merely substituted for the sales tax at its present rate of 3⅓ per cent; if VAT is to confer any significant benefit it must be at a rate which will provide a real incentive to increased efficiency and must be associated with other fiscal reforms with the same objectives, on the lines contemplated in the hypothetical scheme.

CHAPTER IV

VAT AND INCOME TAX

35. It is in the context of a move away from direct taxation that VAT would assume the greatest importance. It is pertinent to recall here that the success of VAT in France, in relation to modernization and exports, stemmed in great measure from the disincentive effects of the taxes it replaced, and it is clear that to achieve success, where no particular disabilities already exist, the introduction of VAT would have to be accompanied by other fiscal reforms.

THE EFFECT ON EFFICIENCY

36. Other things being equal, the more efficient an enterprise the more profit it makes; and disregarding the effect of assessed losses, etc., the more profit an enterprise makes the more income tax it may expect to pay. It can thus be argued that, broadly speaking, income tax is a tax on efficiency. Conversely a tax on costs instead of, or as well as, on profits, might be regarded as a tax on inefficiency. To take a simple example: manufacturer A sells a product for a price of £100; his costs are £40 so that his profit is £60. His income tax is assessed on £60. Manufacturer

B is less efficient: his costs are £60 so his profit is only £40 and his income tax liability is related to this latter figure.

37. Most producers and traders are concerned to improve profit levels and to this end the search for improved methods and greater efficiency is a continuing process. However, where there is a tax on profits the usual consequence of increased profits is the payment of additional tax. Accordingly taxation on profits does not encourage increased efforts towards efficiency. Where there is a tax on costs, on the other hand, the incidence of taxation is complementary to the businessman's natural aspirations; he has an added incentive to reduce costs and thereby both minimize his tax and maximize his profits.

38. Competition is naturally a driving force in this situation. Where there was little or no competition businessmen might be tempted to pass on the whole VAT to consumers, even where they enjoyed a reduction in income tax, and in these case the incentive to increased efficiency would be lost. Nevertheless, although the Rhodesian economy is not as sophisticated in this respect as that of more developed countries, the Committee does not believe that the introduction of VAT would give no encouragement at all to increased efficiency; and if there was an improvement in efficiency over only a part of the field of business enterprise in Rhodesia the economy would benefit.

39. Value added is normally taken to embrace profit and the value added tax therefore includes a charge on profits as well as one on costs. Since the tax is levied on total value added any saving by way of a reduction in costs would, where price remained constant, merely inflate profits by a corresponding amount; thus the tax saved on the cost element would simply be transferred to the profit element. There are, however, a number of points to be borne in mind; firstly if it is accepted that a tax on profits (such as income tax) provides no incentive to profit-making and efficiency, then a tax on net profits plus costs would be preferable to a tax which yielded the same total revenue but which was imposed on profits alone; secondly, the rate of value added tax is normally very much lower than the rate of income tax, and therefore any adverse effect it might have on profit-making and efficiency is that much less pronounced; and thirdly, in the case of export production the tax can be remitted altogether.

40. Where the businessman was unable or unwilling to absorb the tax by reducing his costs and/or profits, he would pass on all or part of it in the form of increased selling prices. To this extent the tax would become a tax upon consumption and could have consequential effects on the cost of living and wages, which would in turn be mitigated by any concurrent reductions in the direct taxation of individuals. The effects of VAT on prices and wages are discussed later in this report.

EXEMPTIONS AND DIFFERENTIAL RATES

41. It is important to note that if the introduction of VAT is planned to coincide with a reduction in income tax there could be objections in principle to allowing exemptions on goods consumed locally: the effect of exemptions is that a producer or trader in exempt goods is relieved of the income tax on profits but suffers no VAT and he is thereby given a tax advantage over other businesses. This advantage is deliberately planned in respect of exports, as an inducement, but would need an entirely different justification in the case of internal business transactions. The only logical case for exemption might be where a limit of application, say £5,000 on goods and £1,000 on services, is set in order to allow the state to avoid

costly but relatively unrewarding administrative processes. Here the trader would pay tax on his purchases, but would neither pay tax on his sales nor be entitled to the deduction. The Committee was also opposed to exemptions on the grounds that they would give rise to anomalies and considerable administrative difficulties, both for registered operators and for the tax administration, as has happened in the case of sales tax.

42. The Committee felt that if the Government wished to take special steps to hold down the price of particular commodities, such as basic foodstuffs, this should be done in other ways than through exemptions under the turnover tax system.

43. The Committee noted the attraction of differential rates of tax as an economic regulator but was opposed to them for three main reasons: firstly, it would be necessary for every invoice specify the amount of tax paid on each article sold, thus seriously complicating the accounting procedures throughout the system; secondly, it would be necessary to define, with minute attention to detail, the classes of goods to which the differing rates would apply; and thirdly, difficulties similar to those experienced with exemptions would arise in any attempt to confine the differential rates to particular lines of trade. In rejecting the idea of differential rates the Committee noted that there were other means of achieving the same objects, for example through selective excise duties, without complicating the administration for commerce and industry.

THE EFFECT ON INVESTMENT

44. The main attractions to capital are political and economic stability and high returns after the payment of tax. VAT's contribution to political and economic stability would of course be only indirect, but if its introduction were to lead to a generally higher level of efficiency and a reduction in taxes on profits this would be a definite attraction to private investment capital, and not only would existing resources be more fully exploited but projects hitherto regarded as uneconomic could be profitably developed. Rhodesia is likely to require external private capital for many years to come and the introduction of VAT, together with its associated fiscal reforms, would be likely to help to improve Rhodesia's competitive position as a field for investment.

45. A reduction in direct taxation would tend to encourage immigration, particularly of people with money to invest.

THE EFFECT ON EXPORTS

46. There are clear advantages to a producer in a system where there is no tax on the profit from exports, and where furthermore the normal tax upon the cost of production is rebateable on goods exported. This is the extreme case but it will be evident that any move in this direction must be beneficial; and that the further the change of emphasis is taken the greater the advantage gained by the exporter.

47. In practice the exporter would pay no tax on the value he has added but he would still receive a credit for the tax which had already been paid by his suppliers of goods and services. The direct export benefit would accrue to the last person in the chain, i.e. the last beneficial owner in Rhodesia. Nevertheless, generally speaking, contributors to the final product would share in this benefit, not through any artificial method of special direct payments to them, but through the natural workings of business which would ensure that each participant's share was reflected in prices throughout the system.

48. It is said that export profitability is sometimes low. If this is so even a tax on costs instead of profits could be an advantage

but where the system went further and the tax on costs was remitted, the advantage would be magnified.

THE EFFECT ON CONSUMER PRICES

49. One of the most difficult problems of the whole subject was to decide what was likely to happen to consumer prices, and following on from that, what would be the effect upon wages and employment, or upon demand and savings where wages remained constant.

50. The Richardson Committee in Britain investigated this aspect very fully, and came to the conclusion that the abolition of the tax on profits would on its own be unlikely to reduce prices quickly to any significant extent; that, on the other hand, a turnover tax was likely to be carried forward as quickly as possible in price; and that on balance, therefore, prices were likely to rise. Against this view, Mr. Anthony Mitton, a British economist and industrialist, argued strongly the other way in his booklet "A Tax for Our Time". Mr. Mitton asserted that the Richardson Committee had misconceived the VAT as a consumption tax and went on to say that there was evidence that businessmen looked to a profit norm based on what they needed to keep their businesses running. If this is the case (and Mr. Mitton's experience is that it is) profit is not a residue, but an essential component of price and the taxation of profits does therefore affect prices. Mr. Mitton concluded that there need be no price rise because the beneficial effects of the tax would soon take over and continue to operate. The Committee took evidence from a few businessmen on this point and the general reaction was that initially there would have to be some increase in prices but that the income tax saving would be taken into account before the amount of VAT to be passed on in price was determined.

51. As has already been demonstrated, the Committee's conclusion is that VAT is a hybrid. It is correct to say that VAT should be regarded mainly as a tax on costs plus profits, but this is not its only property. For reasons already given, a part of the tax is likely to be passed on and prices would tend to rise. The immediate reaction to the joint reform of direct and indirect taxation would probably be one of caution to see that profits were not affected, a sort of trial and error to see how things turned out. The incentive to cut costs in order to reduce the impact of tax would be present at the outset but the translation of possible measures into reality would take a little time. Sellers might be expected, therefore, to take the safe line until the influence of competition and consumer reaction made their weight felt and brought more urgency to the implementation of measures to reduce costs. Such pressure as did emerge would not be evenly distributed, nor would it be the only pressure: the general trend of prices is upward and the tax reform, at most, would add force to other factors.

52. The effects of a reduction of income tax would by no means be all-embracing. Many enterprises do not pay income tax at present, whereas the tax on costs would fall impartially upon every enterprise. To the extent that an enterprise could see no income tax savings to cushion the effect of VAT, its scope for absorbing the increased costs would be limited; but it would realize that the sooner it reduced costs and increased efficiency the quicker it would begin to participate in the greater benefits, by way of profits, that would flow from those measures.

THE EFFECT ON WAGES

53. Applying the hypothetical scheme, and assuming that there would be no exemptions and that the tax would be passed on in full at each stage, the Committee found that the

net result of the tax changes upon consumers could be an increase in the cost of the average family budget of some 2¾ per cent. for Europeans and some 5½ per cent. for Africans. A cross-check employing global calculations confirmed that these were the worst possible effects at the lower income levels and that the overall average effect would be an increased burden of not more than 1½ per cent., due to the fact that the net tax burden would actually decrease in the high income range.

54. The effect on wages of price increases caused by the tax being passed on in some measure is difficult to determine because no specific price increases can be assumed. Any increases that did occur would encourage demands for higher wages, but it must be borne in mind that the cost of living rises steadily and the pressure of rising costs would merely be aggravated by the incidence of VAT. It would not be a calculable or separate factor in the general progression of price increases.

55. The possible increase in consumer prices must be measured against the normal trends of consumer prices and wages. Over the past ten years the European consumer prices index has risen at an average rate of 2.5 per cent. per annum, whereas salaries and wages have increased at an average rate of 3 per cent. per annum. Since 1961 the average annual rise in the African consumer prices index has been 2.6 per cent., whereas wages have increased at an average annual rate of 5.2 per cent. In the case of urban African families, who are likely to be those most affected by an increase in consumer prices, the average annual wage increase has been several times greater than the average annual increase in consumer prices. For example, African wages in the manufacturing industry and in the distributive trades have risen by over 8 per cent. per annum on average over the past five years.

56. Thus the worst possible increase in consumer prices arising from the introduction of VAT is not large in relation to the normal annual movement in wages and prices. It is, however, sufficiently large to justify giving consideration to phasing the introduction of the tax over, say, three or four years. If this were done the effect of the tax on prices in any one year would be less noticeable.

57. In view of the likelihood of some extra costs to consumers the Committee examined the effects on the family budget (see paragraph 53) which would result from the retention of exemptions for basic foodstuffs. The rate of tax would obviously have to be increased in order to maintain the total tax yield, and on the basis of an increase to 8¾ per cent. the net increase in costs would rise slightly to 2.85 per cent. for Europeans, but would fall to around 3⅓ per cent. for Africans. It is again emphasized that these represent the worst effects at a few points in the lower and middle levels of a large range of incomes. In the higher levels the result would be a smaller decrease in the net tax burden because the total amount of VAT paid would rise whilst the saving on direct taxes remained static. As was mentioned earlier the Committee does not favour exemptions and suggests that consideration should be given to arranging the phasing of the reform of the tax system in such a way that the present sales tax exemptions are removed at an early stage.

THE EFFECT ON EMPLOYMENT

58. In the context of the Rhodesian economy, where the availability of unskilled labour is still at a high level, and where a large amount of this type of labour will continue to be offered for some time to come, the effects on employment assume a greater importance than they would in a more developed economy.

59. In the twelve years from 1954 to 1965

the relative shares of earnings and profits in the national product have remained constant. This has leen achieved at the expense of a declining rate of absorption of labour and is due to greatly increased productivity accompanied by an increase in both average and real earnings. This was especially noticeable in the mining sector where despite a large rise in the amount of profits the balance with earnings was maintained, albeit at the expense of employment which actually fell. It will be seen that certain forces are already at work in the field of employment and that if VAT achieved the object of increasing efficiency and productivity it would simply add strength to these existing forces.

60. There are two main problems associated with VAT's effects on employment. First, since VAT, in its role as a tax on costs, would encourage efforts towards greater efficiency, labour would come under scrutiny in the search for cost reductions and improved methods. If increased productivity of labour and greater capitalization were not accompanied by a corresponding increase in the volume of production there would be some unemployment or at least a further decline in the rate of absorption of labour; however, it would be reasonable to expect that the volume of production would also rise, especially if VAT succeeded in accelerating the development of exports, and that further employment opportunities would thus be created. Second, if price increases brought about by VAT were to generate demands for higher wages, businessmen would intensify their scrutiny of labour requirements as part of their general investigation into ways and means of absorbing the higher costs involved.

61. It is unlikely that there would be any serious redundancy if VAT were implemented in stages because the effects on prices would not be such as to justify wage increases in excess of those which would occur in the normal course. Obviously any harmful effects on employment would be mitigated if VAT were introduced on a rising economy.

THE EFFECT ON DEMAND AND SAVINGS

62. If prices rose and earnings remained static there would be a contraction in demand, especially at the lower levels where little or no saving is possible. At the higher levels there might be some contraction in saving at the outset under the initial impact of any increase in consumer prices, but this would disappear as the effects of the income tax reductions made themselves felt. Generally speaking it seems reasonable to expect that overall there would not be any severe impact on either demand or savings.

REGRESSION

63. It is sometimes argued that turnover taxes are regressive in that they fall equally on purchasers of articles which are affected by the tax, regardless of their means to pay. In examining this objection the Committee felt that it was wrong to consider just one part of the tax system in isolation; the tax structure must be regarded as a whole, together with its consequential effects on the welfare of the country and its people. The Committee's opinion was that although a narrow view of the changes outlined in the hypothetical scheme might cause them to be regarded as regressive in nature, a wider view, taking in their longer term effects, could lead to the opposite conclusion.

THE EFFECT IN RELATION TO FISCAL POLICY

64. One important advantage of VAT should be noted in relation to the accrual of revenue to the fiscus. Since turnover moves from year to year less erratically than profit the receipts from VAT are likely to be more stable in the long term than those from in-

come tax. Furthermore, indirect taxes such as VAT can be used much more effectively than income tax as an economic regulator since changes in the level of tax can be brought to bear more quickly.

CHAPTER V

THE EFFECTS ON THE MAIN SECTORS OF THE ECONOMY

PRIMARY INDUSTRY

65. The Committee examined in some detail the possible unfavourable effects of the proposed changes upon the primary industries. Several points were brought to the Committee's attention:—

(a) profitability in this sector is generally low and there are many marginal producers; in these cases increases in costs could be harmful and might force farmers off the land or miners to close their workings;

(b) VAT could strike costs in two ways: by increasing the price of input items, especially where there were monopolies in the sources of supply or where the tax was passed on in whole or in part, and by forcing up wages;

(c) many enterprises in this sector do not pay income tax now, and although those who do might be responsible for a major share of total production, the rest could not absorb cost increases in savings on income tax:

(d) the price of the product is generally difficult to vary due to Government intervention for various reasons in the local market or because export prices follow world market conditions over which the seller has no control.

66. The Committee agreed that there was some force in these arguments but considered it was important not to exaggerate the adverse effects. For example, so far as input costs are concerned the Committee accepted that the whole or part of the tax might be passed on to the primary producers but it considered that these industries have sufficient power, certainly in the long run, to counter undue price increases resulting from monopolies. Furthermore, the Committee could not accept unreservedly the suggestion that such increases would overburden the cost of both materials and manpower. Insofar as the fear of increases in input costs stemmed from the possibility that wage increases would force suppliers to raise their prices by a greater amount than their liability to VAT, the Committee felt that this view did not take sufficient account of the likelihood that suppliers generally would offset at least some part of VAT itself against their income tax savings; thus, having regard to the fact that producers would be able to recover the full tax paid on input purchases, the Committee considered that there need be no significant rise in the cost of these items. As regards the possibility of primary producers being faced with wage demands the Committee has concluded earlier in this report that although the cost of living affects wages it is only one of many factors doing so; indeed increased productivity has been responsible for by far the greater part of increased earnings over the last twelve years. If productivity continued to keep ahead of the cost of living, then the natural increase in wages would absorb any adverse effects of price changes. Such a chain of events could not fail to be advantageous to the economy as a whole.

67. Again as to the question of the farmer's scope for making prices increases himself, he has admittedly, in the case of some products, smaller margins within which to work than the manufacturer. In cases where prices of locally consumed farm products are subject to Government control, and where the introduction of VAT would result in a justifiable price increase, the Committee felt that Government would be under an obligation either to allow such an increase or to assist the farmers concerned in some other way, e.g. by subsidy. So far as export returns are concerned, these depend upon world demand and supply but the effects of this are not always bad. Fluctuations in world prices sometimes operate to the producers' advantage. In any event no VAT would be payable on exports while the tax on input purchases would still be recoverable, and purchases might be cheaper where suppliers did not increase their prices by the full amount of VAT or where the change in the tax structure resulted in improved efficiency amongst those suppliers.

68. There is a special problem in relation to gold and it is envisaged that all gold produced in Rhodesia would have to be treated on the same basis as an export.

69. The Committee does not believe that the primary industries have reached maximum efficiency, and since the profit motive is as strong amongst farmers and miners as with other businessmen, any incentive to increased efficiency would be to their long-term benefit. However, it is accepted that VAT might not exert the same influence here as it would in secondary industry.

70. The Committee examined the effect of VAT on African farmers in the Tribal Trust Lands. Government policy is directed at bringing these farmers into the money economy and the introduction of VAT must not be allowed to impede this process. The main problem would be the increased cost of input items; since the tribesmen would not qualify as registered operators, they would not be able to recover the tax element in their purchases of implements, fertilizers, seed, etc. The Committee agreed that the tribesmen should be assisted to overcome this difficulty, but felt that it was not in a position to suggest the means by which this could best be done; this was rather a matter for Government to consider in the context of the wider problem of bringing the tribal farmers out of the subsistence economy into the money economy.

SECONDARY INDUSTRY

71. The greatest impact of VAT would be in the direction of providing incentives to efficiency, investment and export development in the secondary industries. The profit motive already encourages the attainment of some if not all of these objectives and if VAT has the desired effects it cannot fail to reinforce the existing incentives.

72. The added incentive to modernization and efficiency stands out very clearly. To the extent that VAT is a tax on costs it would reward cost reductions with complementary tax reductions. To the extent that VAT was combined with reductions in direct taxation, investment opportunities in all sectors of industry could become more attractive with beneficial effects on production, exports and employment.

73. In the sphere of exports VAT and its associated fiscal reforms have elsewhere proved to be a positive incentive and there seems no doubt that they could provide the answer, in Rhodesia, to a most difficult problem which cannot be solved satisfactorily by adjusting the income tax law. With a fundamental change in the tax base the net profitability of exports after tax could be improved without any complementary burdening

of production costs. The increased throughput thus made possible could work to the further advantage of both domestic and export profits.

DISTRIBUTION

74. Trade generally tends to find its own levels and only the least efficient stages of distribution are likely to fall away. This would not necessarily be bad and the distributive sector should be able to turn VAT to its advantage in much the same way as other sectors. The scope for increased efficiency might not be as great in the field of distribution as it is elsewhere but at least the incentive would be there, especially since the strength of competition is felt most at the retail level. The Committee would not expect any abnormal increase in prices to be generated at the distribution stage.

SERVICES

75. The inclusion of services within the scope of VAT is an essential part of any plan to widen the tax base. Because services do not attract sales tax at present it might be expected that price increases would be greater in this sector than in those whose products are already subject to sales tax. This is particularly likely to happen in the case of the public utilities, such as the Railways, which do not pay income tax and which would thus have no income tax savings against which a part of VAT could be absorbed. A number of other services, however, include large income tax payers and their ability to absorb all or part of VAT would be much greater.

CHAPTER VI

ADMINISTRATION

76. The Committee was unable to investigate the administration of VAT in every detail because this is a task which cannot be undertaken until Government has made a decision whether or not to introduce the new tax. Instead it examined, through a subcommittee, the main administrative processes and problems associated with the introduction of VAT in a form which the Committee envisaged might be adopted. A major assumption was that there would be a single rate of tax payable at a fixed percentage of the taxpayer's total turnover with no separate specific charge to the customer in respect of the tax. On this basis it appeared that a relatively simple system of administration would be feasible. The fundamentals of the scheme envisaged by the Committee deal with the following:—

(a) registration and qualifications therefor;
(b) definition of turnover;
(c) deductions and refunds;
(d) accrual and payment of tax;
(e) accounting procedures.

REGISTRATION AND QUALIFICATIONS THEREFOR

77. Liability to register, and thus to pay the tax, would be confined to any person who carries on the business of selling goods, whether bought, manufactured or produced by him, with an annual turnover of £5,000 or more, or the business of selling services with an annual turnover of £1,000 or more.

78. Registration would no detpend upon the holding of any particular business licence but simply on the level of turnover. A person engaged in the sale of both goods and services would, if required to register for one, be

liable to pay tax on both. Voluntary registration would be permitted in the case of persons with less than the minimum levels of turnover mentioned above.

79. As to services, the Committee accepted as a general proposition that these should be included in the scheme but did not examine in every particular the complete range of transactions involved. The taxable content of several types of businesses, notably finance, banking and insurance, will need to be examined in considerable depth if and when more positive planning begins.

DEFINITION OF TURNOVER

80. Turnover would be defined as the total amount which accrues to a registered operator from the sale of goods and the provision of services and would include—

(a) deposits against the purchase price of goods or services, less any such deposits refunded;
(b) compensation or damages for breach of agreement or recoveries from insurance against losses;
(c) interest on instalment sales;
(d) the value of goods or services converted to the operator's own personal use or to the use of other persons otherwise than by sale;
(e) the value of accruals from the transport business other than the portion which represents journeys outside Rhodesia;
(f) agency commissions;
(g) auctioneering commissions;
(h) hire charges;
(i) rents;
(j) deposits for returnable containers.

81. Generally speaking sales of a capital nature would be subject to the tax but there are problems associated with these transactions which will require more detailed investigation. Some of the aspects needing further study relate to business assets, including patents, leases and goodwill, and buildings upon transfer of ownership.

DEDUCTIONS AND REFUNDS

82. Deductions in respect of input purchases, exempt sales and exports would be made monthly from turnover. The French system of accumulating credits would not apply and instead refunds would be made monthly where tax payable was less than the credit for tax on purchases.

ACCRUAL AND PAYMENT OF TAX

83. Tax would fall due at the time of a transaction but would only be payable within, say, thirty days of the close of the month's business. Liability to tax would be on an accruals basis and would not be affected by bad debts.

ACCOUNTING PROCEDURES

84. A simple monthly return would be necessary. This would take the form of a tabulation of total turnover with provision for the deduction of exports and such goods and services as may be exempt; a deduction in respect of purchases from registered operators; and finally, a calculation of the net tax payable by, or refundable to, the registered operator.

85. In support of this return operators would be required to maintain a register of purchases and sales, isolating where relevant the operator's purchases from nonregistered persons. All invoices issued would be required to bear the seller's name and registered number and in their absence deductions claimed by the purchaser would be disallowed. Exports would be proved by the submission of customs and transport documents.

GENERAL

86. A countervailing tax would have to be imposed upon imports and this would be at

the same rate as the tax on domestic transactions. The value for tax purposes would be the sum of the value for customs duty purposes and the customs duty itself.

87. In many cases services provided to ratepayers by local authorities are charged to the authority's general rates fund and no specific charge is made; in other cases separate charges are payable. Provision must be made for these services to be exempt from the services tax.

88. It is emphasized that the scheme outlined in this chapter is not intended to be complete or final. It is given merely as a guide to some of the most important matters which will have to be covered in the more detailed planning, if and when VAT is adopted. Although this scheme would involve more administrative work than the present sales tax, the Committee considers that the arrangements described represent a relatively simple and efficient process which need not impose an insupportable burden upon persons liable for the tax. In some cases bookkeeping may have to be extended in scope and improved in quality. Where this occurs it must surely be rated as a contribution to increased efficiency.

89. It is envisaged that test checks would be undertaken and that penalties would be imposed for contraventions of the law.

90. The Department of Taxes already operates an administration which examines business turnovers and the Committee takes the view that this Department, rather than the Customs Department, would be best suited to control and administer VAT. The inspection and accounting staff would have to be increased but even so it is not thought that VAT would be an expensive tax to administer.

CHAPTER VII

CONCLUSIONS

91. The Committee does not believe that there is any advantage to be gained from VAT merely as a substitute for sales tax at its present rate. The major benefits could be attained only if VAT were introduced as part of a complete review of the whole tax system.

92. The Committee has no doubt that if Rhodesia had a highly developed and sophisticated economy the introduction of VAT, coupled with the other fiscal measures envisaged, would achieve beneficial results. The question is whether it would be of advantage while the primary industries still occupy a prominent position and while competition in some sectors of business is limited. The Committee was impressed by the argument that the advantages of VAT for the primary industries, especially for individuals as opposed to companies, would be very much less marked than for other sectors; indeed in some cases there might even be a positive disadvantage. The introduction of VAT might also, in the short term, have an adverse effect on consumer prices.

93. As to the effect of the introduction of VAT on the economy as a whole, the Committee cannot prove conclusively that it would be to Rhodesia's advantage to make the change; neither, on the other hand, can it adduce any firm figures indicating that it would be to Rhodesia's disadvantage. It is, however, the Committee's feeling that in the long term a tax system which tends to reinforce the businessman's natural urge to

reduce costs and increase profits must bring benefits to the economy as a whole.

94. A major reconstruction of the tax system, whether it be through the introduction of VAT or any other major tax change, is bound to involve a period of adjustment which may bear hardly on some sectors of the community. If a major change is accepted as being desirable in principle, therefore, the problem is to mitigate the harmful side effects which could occur during the period of transition.

95. The Committee believes that there are three main ways in which this problem could be overcome in the case of VAT. Firstly, the changes could be implemented over a period of three of four years so as to ensure that any specific pressure on consumer prices as a result of the introduction of VAT would be dissipated in the normal upward trend of prices; thus the disadvantages of VAT insofar as they relate to consumers and to wages, particularly in the primary industries, could be kept to a minimum. Secondly, the phasing could be timed to coincide with a rising trend in the economy. And thirdly Government could give assistance to those sectors of the economy which encountered serious difficulties in passing through the transitional period, provided it was satisfied that this was in the interest of the economy as a whole. This assistance could take various forms, depending on where the need was felt and how it could best be satisfied, and might include direct subsidies or the remission of existing taxes such as mining royalties.

96. The Committee regards phasing as a most important aspect of any scheme and gave some thought to how this could be applied to the hypothetical scheme. Certain modifications to this scheme appeared to be necessary and were incorporated in a draft phasing programme, details of which are contained in the Appendix to this report. The question of phasing is of course one for Government to consider further if it decides to implement VAT, but the Committee feels that something along the lines of its draft would go a long way towards mitigating the transitory effects which have been referred to. On the other hand it must be recognized that phasing would cause difficulties for the business community and from their point of view fewer stages would be preferable.

97. It is important to emphasize that no sudden miracle can be expected from the introduction of VAT. Its adoption, together with the other fiscal reforms suggested in this report, must be regarded essentially as measures for the long term benefit of Rhodesia as a whole and there should be no expectation of quick results. Nevertheless, the sooner a start can be made the sooner the benefits will begin to flow.

98. To summarize, therefore, the Committee has come to the conclusion—

(1) that is likely to be advantageous to Rhodesia's long term interests to introduce VAT and the associated fiscal reforms outlined in this report;

(2) that the introduction of these measures should be phased over three or four years;

(3) that their introduction should be timed to coincide with a rising trend in the economy;

(4) that the Government should be prepared to give assistance to those sectors of the economy which meet serious difficulties in passing through the transitional period, provided it is satisfied that the granting of such assistance is in the interest of the economy as a whole.