

TAXATION
OF
FOREIGN AND NATIONAL ENTERPRISES
(Volume II)

**STUDIES OF THE TAX SYSTEMS AND THE
METHODS OF ALLOCATION OF THE PROFITS
OF ENTERPRISES OPERATING IN MORE THAN
ONE COUNTRY.**

**AUSTRIA, BELGIUM, CZECHOSLOVAKIA, FREE CITY OF DANZIG,
GREECE, HUNGARY, ITALY, LATVIA, LUXEMBURG,
NETHERLANDS, ROUMANIA AND SWITZERLAND.**

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PREFACE

This volume contains a study of the system of income taxation of twelve European States from the point of view of enterprises doing business in more than one country. Together with a similar volume dealing with the legislation of a certain number of non-European countries,¹ it is the result of an enquiry of which the first findings were published in a volume entitled "Taxation of Foreign and National Enterprises in France, Germany, Spain, the United Kingdom and the United States of America".

This enquiry, which was undertaken thanks to a grant from the Rockefeller Foundation, had for its principal object the study of the methods actually employed for the allocation or apportionment of the income of enterprises having establishments in countries other than that of their fiscal domicile. Its purpose was to provide the Fiscal Committee with the data necessary for formulating a draft convention for the avoidance of the double taxation of business income.

These data were submitted to the Fiscal Committee at its fourth session in June 1933, together with a study by Mr. Mitchell B. CARROLL, director of the enquiry, entitled "Report on the Methods of allocating Taxable Income",² which consists, on the one hand, of a general survey of the methods of allocation practised in the different countries and, on the other, of the practical conclusions tending to indicate which system of allocation would appear most suitable for general adoption. This documentation was completed by a study by Professor Ralph C. JONES, on the accounting aspects of the allocation of the income of industrial enterprises.³

On this basis the Fiscal Committee has framed a draft Convention, which it adopted on June 26th, 1933, and which is principally intended to serve as a model for bilateral and even multilateral conventions.

A pre-requisite for an examination of the methods for allocating business income as well as the method of taxing the different items of income is a knowledge of the system of direct taxation in each of the countries under review. Each report contained in the two volumes now being published, as well as those which appeared in the 1932 volume, is divided into three sections :

1. A survey of the income tax system and, for those countries where it exists, the property tax system.
2. A survey of the methods of taxing the various items of income (interest, dividends, royalties from patents and other intangible property, income from real property, salaries and wages, business income), according to whether they belong to foreign or national enterprises or whether they arise from foreign or national sources.
3. Finally, a last section in which is examined, first, the provisions applicable to the taxpayer's books and accounts ; secondly, the use of the different methods of allocation (separate accounting, fractional apportionment, empirical methods) ; and thirdly, the manner in which gross profit, interest, general overhead and net profit are apportioned between the branch

¹ *Taxation of Foreign and National Enterprises* — Volume III : British India, Canada, Japan, Mexico, Netherlands East India, Union of South Africa, States of Massachusetts, of New York and of Wisconsin. (L.O.N. document C.425(a).M.217(a).1933.II.A.)

² Volume IV of this collection. (L.O.N. document C.425(b).M.217(b).1933.II.A.)

³ Volume V of this collection. (L.O.N. document C.425(c).M.217(c).1933.II.A.)

and the real centre of management. This section is completed by a study of concrete cases : an examination is made of the manner in which the rules set forth in the preceding paragraphs are applied to the different kinds of enterprises, such as industrial and commercial enterprises, banks, insurance companies, railways, electricity and gas companies, telephone companies and mines.

The outline indicated above has been followed in each of the studies undertaken in the course of the enquiry, and for this reason it should be easy to compare the various tax systems point by point. It also makes it possible to complete, when necessary, the material synthesised in Mr. Carroll's study and to ascertain to what extent the adoption of the rules advocated by the Fiscal Committee would confirm or modify the practices now followed in allocating profits.

The studies contained in this volume have been prepared either by the members of the Fiscal Committee or, under their direction, by officials in the fiscal administrations of the different countries. The names of the authors are to be found on the title-page of each study.

AUSTRIA

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PART I. — GENERAL DESCRIPTION OF INCOME-TAX SYSTEM.¹

The Austrian federal direct taxation system is made up of certain direct taxes on receipts and income from landed property and buildings, from business undertakings, from services performed for another, from the investment of capital and from other sources.

These taxes are : The income-tax (*Einkommensteuer*), the general tax on profits (*allgemeine Erwerbsteuer*), the tax on salaries (*Besoldungssteuer*), the company tax (*Körperschaftsteuer*), the tax on capital yield (*Rentensteuer*) and the tax on directors' percentages (*Tantiemenabgabe*).²

Since the great fiscal reform of 1896 (Law of October 25th, 1896, relating to personal direct taxes, *Federal Law Bulletin*, No. 220), the Austrian direct taxation system has consisted of a number of taxes on receipts (*Ertragsteuern*), together with a tax on the whole income. The schedular taxes are designed to meet the actual contributive capacity (based on economic yield) of the various sources of schedular income. The income-tax, on the other hand, is adapted to the personal consuming capacity of the taxpayer — that is to say, it takes account of certain social conditions when estimating the taxpayer's contributive capacity. By these two groups of taxes, fulfilling different functions of fiscal policy, the Austrian fiscal system seeks to effect an equitable distribution of the burden of taxation. Since 1923, schedular taxes have not been levied only by the Confederation, for the various provinces now impose taxes upon income from landed property and buildings (real taxes), and each province has its own system of collection. These taxes are, however, in principle, still an integral part of the system of schedular taxes.

The following are the features of the federal taxes on income and receipts (Personal Tax Law, *Federal Law Bulletin*, No. 307, 1924, together with subsequent amendments) :

(a) *The income-tax* is, in principle, levied on the whole of the actual net income of persons domiciled or permanently resident in Austria. In the case, however, of certain income derived

¹ Legislation in force on May 1st, 1933.

² The following are the figures in the 1933 federal budget showing the estimated revenue from these taxes (in millions of schillings) :

Income-tax	120
General tax on profits	34
Tax on salaries	16
Company-tax	36
Tax on capital yield	21
Tax on directors' percentages	2
	229

Since the total fiscal revenue in the federal budget of 1933 is estimated at 1,068 millions of schillings, the above taxes represent over a fifth of the national revenue from taxes. The State pays over part of this revenue to the provinces and communes (Law on allocation of fiscal revenue [*Abgabenteilungsgesetz*], B.G. Bl., No 62, ex 1931).

from foreign sources (income from real property, from business undertakings and from State funds), the law allows this income to be deducted from the assessed amount payable in Austria by a taxpayer living in that country. This deduction, however, is only allowed where a similar tax is imposed abroad and where the foreign country concerned accords reciprocity of treatment to Austria. On the other hand, every individual is taxable in Austria, regardless of domicile or place of residence, in respect of certain income derived from Austrian sources — income from landed property, from mortgages, from investments, from business undertakings or from participation in such business, from funds administered by the Confederation, provinces, districts and boroughs, and, lastly, from fees of company directors.

Incomes not exceeding 1,400 schillings per annum net are exempted. The underlying principle of the law is that account must be taken of the household, and to the income of heads of households must be added that of the other members of the household. The tax is graduated on a sliding scale rising on a percentage basis from 1.1 per cent to 4.4 per cent and attaining thereafter, still on a graduated scale, a maximum of 45 per cent. (Table of Tariffs, Annex.) In the case of taxpayers not liable in respect of their whole income — *i.e.*, those liable solely in respect of income from Austrian sources — the income-tax, when the total taxable amount does not exceed 1,400 schillings, is 1 per cent.

The income-tax is supplemented by a *property-tax (Vermögenssteuer)* levied upon the property from which the individual derives an income. A prerequisite for the payment of this tax is that the taxpayer shall already, in principle, be subject to income-tax. The taxable property consists of the total amount of capital assets yielding income subject to income-tax. In the case of landed property used for farming or forestry, the capital value is fixed, in the event of personal administration, at ten times the net income, and, where the property is let, at twenty times that total; in the case of buildings and invested capital, at twenty times the net income; in the case of business undertakings of the second group (see paragraph (b)), at ten times the net income. The capital value of debts and liabilities is fixed at twenty times the abatement allowed under this heading for purposes of income-tax assessment. By reason of this method of assessment, the property-tax serves as an additional income-tax on income from invested capital. The taxpayer is liable on all capital over and above 36,000 schillings on a scale rising in four stages from 0.5 to 3 per thousand. (Table of Tariffs, Annex.)

(b) *The general tax on profits* affects net profits from enterprises operating in Austria and from professional occupations, excluding the profits from enterprises liable to the tax on companies, from salaried occupations and from forestry and agriculture. As regards enterprises operating in Austria, which extend their activities to another country, the profits realised abroad are exempted if they possess an establishment there which is liable to a tax similar to the Austrian general profits or income tax, subject, however, to the country concerned according reciprocity of treatment to Austria. In the case of foreign enterprises operating on Austrian territory either by setting up establishments there or merely by having recourse to other means of doing business, or by acting through commercial travellers or directly in Austria, these concerns are taxable according to the extent of these activities.

The tax is imposed upon individuals or partnerships owning an enterprise. Taxpayers are divided into two groups, the first including the liberal professions and callings requiring personal services, together with concerns and occupations of any other sort in which the use of capital is insignificant relatively to the labour employed. The second group includes all other concerns.

The tax is assessed on net receipts as arrived at for purposes of income-tax. In the case of taxpayers of the first group, the tax is graduated on a descending scale from 4 to 1 per cent, and, for the second group, on a scale of 7.5 to 5 per cent. The minimum tax is 10 schillings. In the case of registered concerns (*protokollierte Firmen*), the tax must equal at least 1.25 per cent of the net assets, but may not be less than 420 schillings. (Table of Tariffs, Annex.)

(c) *The tax on salaries (Besoldungssteuer)* was first introduced in 1931. It affects all individuals who work for others in the capacity of employees and who receive remunerations for present services or retirement pensions liable to income-tax. In the case of wages and salaries, however, liability depends on various factors enumerated below, any one of which suffices to determine liability: the contract of service must be for an unlimited period or for at least twenty years, and must not be terminable at the employer's discretion or by reason of the liquidation or reduction of the concern; or the employee must, at the termination of the contract, be entitled to a permanent pension from the employer; or the employee must be in receipt of a remuneration exceeding 12,000 schillings per annum. Pensions on retirement or disablement are unconditionally liable to the tax.

Persons whose taxable incomes do not exceed 3,000 schillings per annum are exempt from this tax. This exempted minimum is raised to 3,400, 3,800 and 4,200 schillings, according to the number of persons dependent on the taxpayer. Remuneration for services falling within this category is exempt when such income is derived from activities abroad or from pensions drawn abroad, provided that it is liable to a similar tax abroad and that the foreign country in question accords Austria reciprocity of treatment.

The tax is assessed on a scale rising from 1.1 to 10 per cent. (Table of Tariffs, Annex.)

(d) *The company-tax (Körperschaftsteuer)* is imposed on the net income of companies. In determining liability, the law distinguishes three groups of companies.

The first includes Austrian companies by shares, mining companies, mutual insurance societies, co-operative societies (*Erwerbs- und Wirtschaftsgenossenschaften*), limited liability companies, savings banks and public utility corporations (*Gemeinwirtschaftliche Anstalten*). In Part II of this study, concerns in this group will be briefly designated as "profit-earning companies possessed of a legal entity". These companies are liable to taxation regardless of the nature or origin of their net income.

The second group includes the State and the public corporations, together with the legal entities subject to the rules of public accountancy; these collectivities are assessed to taxes in respect of the concerns exploited by them. Exemption, however, is granted to concerns exploited by the State and the public corporations in virtue of sovereign rights (for example, monopolies) or for purposes of public administration.

The third group includes foreign companies of all kinds. The latter are liable to the tax, firstly, in respect of establishments set up by them in Austria, and, secondly, if they belong to the category of enterprise mentioned in the first group, in respect of their real property in Austria and their proprietary interest in Austrian concerns. However, the mere possession of shares and other securities of a similar kind does not of itself constitute a proprietary interest.

In the case of Austrian enterprises operating abroad through foreign establishments, the income accruing from foreign operations is liable to the tax only when it is possible to prove that it is not taxable abroad. If, on the other hand, a foreign concern operates in Austria, the Austrian establishment is liable.

The tax is assessed on the surplus shown on the balance-sheet, regard being had to all authorised deductions and additions. The normal rate of the tax is 25 per cent of the income, but must amount to at least 2.5 per thousand of the paid-up capital. In the case of a number of companies enjoying favoured treatment (particularly savings banks and co-operatives), there is provision for graduated and reduced scales according to total net income. Foreign companies, which are only liable in respect of income from real property in Austria or holdings in Austrian concerns, pay 15 per cent. (Table of Tariffs, Annex.)

(e) *The tax on capital yield (Rentensteuer)* is imposed upon income from property or vested interest when such income is not already liable to the taxes on land and buildings or the tax on profits or the company-tax. Hence, income from capital which is taxed indirectly under the company-tax — for instance, dividends of Austrian share companies — is not liable to the tax on

capital yield. Various exemptions are granted, both *subjective* (confederation and provinces) and *objective* (allowances received from near relatives). More particularly, persons are exempt whose incomes liable to the tax on capital yield do not, either alone or when added to other income, exceed 1,400 schillings (the minimum income liable to income-tax). This minimum is doubled in the case of persons over 60 or persons who are incapable of earning their living. This exemption does not apply when the tax is collected at the source from the debtor.

In the case of incomes derived from abroad, these, too, are exempt from the tax on capital yield when it can be shown that they are subject to a special direct tax abroad apart from income-tax already paid by the beneficiary. Individuals and legal entities not resident in Austria are liable to the tax on capital yield in respect of the entire amount of such income accruing to them in Austria.

Normally, the tax is 10 per cent, but, in the case of certain income (rents), amounts to 15 per cent ; in the case of certain other income, there is provision for a lower rate (on savings-bank interest, 5 per cent ; interest on certain mortgage bonds, 3 per cent. (Table of Tariffs, Annex.)

(f) *The tax on directors' percentages (Tantiemenabgabe)* is levied on the fees of any kind received by the directors of companies by shares (*Aktiengesellschaften*) and limited companies (*Kommanditgesellschaften*) in their capacity of directors. The tax is 10 per cent, plus a federal surtax amounting to twice or three times the tax itself. In practice, the maximum tax is generally 40 per cent.

I. TAXPAYERS.

(a) INDIVIDUALS.

The following are the taxes on the income of individuals : income-tax proper (and, indirectly, property-tax), general tax on profits, tax on salaries, tax on capital yield, and tax on directors, percentages. As stated above, these taxes are imposed only on individuals, with the exception of the general tax on profits and tax on capital yield, which are also imposed on partnerships.

As regards liability for payment of all these taxes, *nationality* is not a determining factor. There is, however, one unimportant exception to this principle, in favour of foreigners — namely, foreign diplomats and their staffs, who are exempt from the income-tax and from the tax on capital yield.

Nationality does, however, play a certain part in the fiscal system obtaining under treaties. Clauses in certain treaties concluded by Austria apply only to subjects of the contracting countries (treaties with the German Reich, *Federal Law Gazette*, No. 286, 1923 ; with Czechoslovakia, *Federal Law Bulletin*, No. 2, 1923 ; and with Italy, *Federal Law Gazette*, No. 341, 1926).

Further, under the terms of the treaties and agreements concluded with Hungary (*Federal Law Bulletin*, No. 437, 1925) and with Switzerland (*Federal Law Bulletin*, No. 96, 1928), the application of which does not, in principle, depend on nationality but on the taxpayer's fiscal position in Austria, the right of one or other of the contracting States to levy tax is decided, in certain cases of double domicile, by the taxpayer's nationality.

Nevertheless, *domicile* and *residence* play an important part in fiscal matters.

The taxpayer is liable for *income-tax* on the whole of his income if he is domiciled in Austria or resides there for more than one year. When these conditions are not fulfilled, a temporary residence for profitable purposes suffices, regardless of length of stay, and the individual is liable in respect of income accruing to him in Austria in the course of such residence (paragraph 153 of the law relating to personal taxation). The law itself does not contain any more precise definition of domicile.

In terms, however, of the executive rules made thereunder, a person is domiciled in the place where he settles with the intention of remaining there continuously, when such intention is apparent or is indicated by the circumstances. A person may have more than one domicile and may, for instance,

be domiciled both abroad and in Austria. As to whether residence has exceeded one year, it is immaterial whether the party concerned has resided in one place or several places, and whether it has been interrupted after a period exceeding one year. The administrative tribunal has ruled that a foreigner having permanent residence in Austria is domiciled there even when he dwells there only for a part of the year. Uninterrupted or exclusive residence is, moreover, not one of the necessary conditions of domicile (Official Collection of the Judgments of the Administrative Tribunal No. 7410, 1910; No. 11607, 1917; No. 12755, 1921).

Liability for the *general tax on profits* is independent of domicile and residence.

With regard to the *tax on salaries*, the same provisions as to domicile — residence for more than one year and residence for purposes of profit — apply as in the case of income-tax.

Generally speaking, liability for the *tax on capital yield* and the *tax on directors' percentages* is independent of domicile and residence. However, individuals and legal entities not domiciled in Austria are, as the result of special legislative provisions concerning loans and interest in foreign currency (*Federal Law Gazette*, No. 50, 1933), exempt from this tax in so far as concerns interest accruing to them from Austrian banks and payable in foreign currency. This exemption is operative until December 31st, 1934.

Under *treaty law*, domicile and residence play a very important part. Under the treaties with Germany, Czechoslovakia and Hungary, the right to impose direct taxes belongs, essentially, to the country of domicile, and, in the absence of a domicile, to the country where the taxpayer is (permanently) resident. The principle of territoriality determines the right to levy tax only in respect of sources of income inherent in the country concerned. Under these treaties, a person is domiciled in any given place when he has a residence there in circumstances implying an intention to reside there permanently. In the case of double domicile, liability is governed by the length of residence, especially where it is a question of the proportional allocation of taxable property.

Under the treaty with Italy, liability is not governed by residence or domicile except for purposes of income-tax levied on income derived neither from territorial sources nor from work. Under this treaty, a person is domiciled in the place where he has a permanent residence in circumstances implying an intention on his part to remain in that place. In the case of multiple domicile, the tax is proportionally allocated according to the length of stay in each of the contracting States.

Under the treaty with Switzerland, income from services performed for another is liable to income-tax in the country of domicile. Where a person is domiciled in both the contracting countries, the tax is imposed in the country where the taxpayer's family is domiciled. Under this treaty, a taxpayer is domiciled in the place where he is living with the intention of residing there permanently.

(b) PARTNERSHIPS.

Here the relevant taxes are the general tax on profits and the tax on capital yield.

Partnerships are liable to the *general tax on profits* in their capacity as enterprises. Consequently, commercial partnerships (*offene Handelsgesellschaften*) and all legal entities are liable, the latter, however, only in so far as they are not subject to the company-tax. Among them are concerns belonging to groups (*Vereine*) not subject to the rules of public accounting. Among partnerships must also be classed joint ventures (*Vereinigungen zu einzelnen Geschäften*). Whether an enterprise consists of one individual or of a number of partners is a question of fact and is not determined by registration in the Commercial Register. Partnerships are liable, as such, to the tax on profits, the taxable income being the total profits accruing to all the partners. *Income-tax*, on the other hand, is levied on each partner separately in respect of his own share of the profits.

Partnerships are similarly liable to the *tax on capital yield*, as such, and on the whole of their taxable income.

(c) COMPANIES.

Here the relevant taxes are the company-tax and the tax on capital yield.

Liability to *company-tax* depends upon whether the company is an Austrian or a foreign company. As shown above (page 12), certain Austrian companies — viz., those of the first group — are by their very nature liable, regardless of whether they operate for profit or not. Other Austrian companies — viz., of the second group — are only liable to taxation if they operate an enterprise. Foreign companies, on the other hand, are never liable to taxation, by the mere fact of possessing legal entity. The latter, before becoming liable to company-tax, must either operate for profit in Austria, or own real property in that country, or possess interests in an Austrian concern operating for profit. The question whether the company is Austrian or foreign is determined by its official place of business (*Formalsitz*), the law containing no express provision on this point. The idea of a “real centre of management” is unknown to the law, which considers that a foreign company, when not already liable by reason of possessing real property in Austria or interests in an Austrian concern, is subject to the company-tax, only when it has an establishment in Austria.

Austrian and foreign companies are liable to the *tax on capital yield* on all income taxable under this head (see explanation given under (a) as to the exemption of foreign legal entities in the case of certain interest on loans). Under fiscal conventions, the right to tax on capital yield is with the creditor's country of domicile, in so far as the tax has not already been collected at the source and, under certain treaties, in so far as this tax is not levied on income from mortgage loans. For this purpose, the treaty with Switzerland provides that companies and legal entities are domiciled at the seat of their real centre of management.

2. TAXABLE INCOME.

The terms “national income” and “foreign income” are not defined either in domestic legislation or in fiscal treaties. Where national enterprises have establishments abroad, the law makes provision for a minimum Austrian income. As regards the general tax on profits, it is provided that at least one-quarter of the whole net income earned by the enterprise shall be deemed to have been earned in Austria. As regards the company-tax, the following proportions of the total income earned by the whole enterprise are liable to the Austrian tax: when the concern is engaged in exchanging goods between home and abroad or *vice versa*, at least one-half; when the goods are produced in Austria and sold abroad, at least two-thirds. In all other cases, at least one-tenth. These minima are not provided for in the fiscal treaties. Only in the agreements concluded with Hungary is it provided that at least one-tenth of total profits shall be taxable in the country in which an enterprise liable to company-tax has its seat of management.

3. ASSESSMENT OF TAX.

(a) COMPUTATION OF TAXABLE INCOME AND DEDUCTIONS.

Taxable amounts are computed differently according to whether we are dealing with income-tax or schedular taxes.

In the case of *income-tax*, the assessment is made on the taxable income actually earned in the course of the year. There is no abstract legal definition of income; the law merely specifies what it regards as taxable income—namely, the total sums accruing to the taxpayer in cash or cash equivalents, including the rental value of his own house or other free accommodation, together with the value of the fruits of his own labour or industry consumed in his own home, but expenses incurred in earning, securing and maintaining the aforementioned income, or interest on debts are deductible. Extraordinary income from legacies, life insurance and capital insurance, from gifts and other property acquired free is not taxable. Revenue derived from the sale of capital is not classified as income except where such sale occurs habitually as a business transaction or takes the form of speculation.

Deduction is allowed, in particular, for administrative and working expenses and maintenance

costs, including depreciation,¹ compensation for damages and life insurance premiums (in the case of the latter only up to a certain sum); further deductions are social insurance premiums, direct taxes paid by the taxpayer (excluding income-tax), interest on all private and commercial debts, together with all permanent charges against income confirmed by legal instrument. On the other hand, no abatement is allowed in respect of expenses incurred in improving and increasing the property, such as capital outlay, business extensions, and debt payments; the same holds good with regard to losses of assets, such as the loss or dwindling of one of the sources of income, unless the particular asset item affected produced the income and there is a direct connection between the loss and the use in question. The same also applies to losses on shares in the business, interest on private capital belonging to the taxpayer and invested by him in a business, housing and upkeep expenses of the taxpayer and his family and, finally, disbursements not incurred in producing the income.

In calculating the annual income from independent enterprises and occupations pursued for purposes of gain, the expenses enumerated above as admissible abatements must be deducted from profits. Taxpayers whose affairs are regularly accounted must reckon industrial and commercial profits according to the legal provisions set forth above and according to existing commercial legislation dealing with inventories and balance-sheets — *i.e.*, in accordance with ordinary commercial practice. Where an enterprise operating for profit is liable to the general profits tax, it is taxable in respect of income-tax on the same total as that arrived at for purposes of general tax on profits.

The net total income taxable under the *general tax on profits* is calculated under the same provisions as those governing income-tax¹. Consequently, interest paid on foreign capital invested in an enterprise, together with the tax on profits, may be deducted; on the other hand, shares in profits paid to silent partners may not be deducted. In the case of partnerships, the net revenue includes the profits accruing to all the partners. Where joint ventures are concerned, profits already included in the net income of an enterprise which has itself been taxed on its profits must not be reckoned.

The basis of assessment for *tax on salaries* is the salary or wage assessable to income-tax.

The *company-tax* is assessed on the net trading revenue for the financial year ending during the course of the fiscal year. This revenue consists of the active balance after adjustment of all allowances and additions prescribed by law, irrespective of the particular nature of the receipts, whether interest, dividends, directors' percentages, etc., or whether they are put into a reserve fund, carried forward or employed otherwise. The fiscal authorities thus determine the net taxable income on the basis of the surplus in the balance-sheet, subject, however, to certain additions or deductions.

The following are the *additions*: sums devoted to increase of capital, such as sums appropriated to initial installation and investment; refund of capital and debt redemption the effect of which is to increase the concern's assets; sums appropriated to payment of interest on the company's own capital, and interest on ordinary bonds and mortgage bonds; guarantees and subsidies to other concerns; gifts and gratuities not necessary to the conduct of the business; sums appropriated to payment of company-tax and, finally, losses brought forward from previous financial years.

Deductions are allowed in respect of the following: profits brought forward from previous financial years, guarantee payments in hand, reserves of insurance companies to meet premiums and compensation claims, interest on debts in so far as it is not interest on the company's capital especially discount interest, interest on deposits and interest on unsecured loans; sums written off

¹ The so-called laws "in favour of capital investment" (*Investitionen-begünstigungsgesetze*) contain special provisions for the writing-off of especially large sums. The effect of these provisions so far extends only to 1932. They allow the amortisation, in advance and tax free, of 50 per cent of the expenses of capital investment. In the case of taxpayers who keep no regular accounts, this proportion is reduced by 25 per cent.

or set aside as a sinking fund reserve¹; compensation payments to staff; payments out of profits made to staff employees under a contract, but excluding percentages to directors.

In sum, there is one essential difference between the company-tax, on the one hand, and the general tax on profits and income-tax, on the other; first, the addition to the assessed tax of sums paid as interest on capital indebtedness and mortgage loans (in so far as these loans and indebtedness correspond to capital employed in the business), and, second, the addition of the sum appropriated to payment of the company-tax itself.

The *tax on capital yield* is, in principle, assessed on the gross annual taxable income. Only exceptionally is it possible to make deductions; deductions for interest on debts are only allowed when the income is derived from a private claim to which there directly corresponds a debt contracted by the creditor or where interest has been paid for the rediscounting of a discounted bill, or in the case of interest charged on current accounts. With regard to income from the lease of goodwills or hunting rights, administration and maintenance expenses (including depreciation) connected with the object leased may be deducted.

The *tax on directors' percentages* is levied on the whole of the income thus acquired without any deduction whatsoever.

(b) COMPUTATION OF TAX AND ABATEMENTS.

Income-tax. — This tax is computed according to a tariff as a percentage of the taxable income.

The following principle is followed: the income in a higher scale must not be less than the largest income in the scale immediately below, after deduction of tax.

On incomes up to 10,200 schillings, scaled abatements are provided in respect of persons dependent on the taxpayer: (a) 5 per cent of the tax for each dependent, (b) reductions up to a maximum of 30 per cent of the tax where the taxpayer's contributive capacity is reduced by special circumstances, and, lastly, complete exemption where the taxable income does not exceed 1,800 schillings.

When the taxable income includes extraordinary revenue in the shape of payment for scientific, artistic or literary work spread over several years, the tax is assessed on the whole income. In these cases, however, the percentage is fixed by dividing the sum received by the number of years over which it was earned. In assessing extraordinary income from timber-felling, only 20 per cent of the additional receipts is added to the usual income. The same applies to single payments made as compensation for lost assets, lottery winnings and other extraordinary income of the same character. Except for income from scientific, artistic and literary work, this provision does not apply to extraordinary revenue derived from the pursuit of normal trading or occupational activities for profit or by way of speculation.

General Tax on Profits. — This tax is computed as a percentage of the net taxable income. As with income-tax, the intercalary scale is employed. Where the net income does not exceed the minimum exempt from income-tax (1,400 schillings), there is a fixed profits tax (between 10 and 80 schillings). In the case of the need, this tax may be reduced or even entirely remitted.

In the case of registered enterprises (*protokollierte Firmen*), the minimum rate is fixed on the basis of net assets; no abatement is allowed, even in respect of dependents.

¹ As to extraordinary sinking funds, see footnote on page 16.

Tax on Salaries. — This tax is computed as a percentage of the taxable total. As with income-tax, the intercalary scale is employed. Gratuities paid on expiry of contract are reckoned in their entirety, though only 20 per cent of such payments is actually taken for purposes of computation. No abatements are allowed, even in respect of dependents.

Company-tax. — This tax is computed as a percentage of the net taxable total. It is fixed on the basis of the capital and, in the case of insurance companies, on the total net annual premiums.

Taxes on Capital yield and Directors' Percentages. — These taxes are always computed as percentages of the taxable income.

The law makes no provision for taking into account, with a view to avoiding double taxation, taxes paid abroad. Under Austrian law and under the fiscal conventions, this result is sought in another way — by separating foreign income from revenue taxable in Austria.

4. COLLECTION OF TAX.

The direct taxes mentioned in this chapter are computed by the federal fiscal authorities of first instance (fiscal administrations, district fiscal authorities) — *i.e.*, committees attached to these authorities. These committees are of mixed composition. Some of the members are nominated by the Finance Minister, others are chosen from among taxpayers by the representative political assemblies (provincial diets, municipal councils) and the remainder by professional associations.

These committees administer the general profits, income and property taxes. The company, capital yield and directors' percentages taxes are administered direct by the fiscal authorities themselves.

Taxpayers are required to make an annual return upon which the tax is assessed. When taxes are deducted at the source, the importance of the return is less. Returns made in respect of all direct taxes, excepting the company-tax, must be presented by March 31st. Returns for the company-tax must be presented not more than six months after the end of a financial year.

The fiscal authorities transmit to each taxpayer a notice (*Zahlungsbescheid*) setting out the amount of tax claimed. In the case of the general profits, income and property taxes, a demand note (*Steuermandat*) is sent to the taxpayer, which the latter may render inoperative by lodging an appeal within three weeks. His case is then heard by the assessment committee. (In the case of the company-tax, the delivery of a demand note is optional and in practice rare.)

The taxpayer is informed by the authorities of the result of his appeal. A further demand is sent to him (*Zahlungsauftrag*) and against this he may appeal within thirty days. The matter is then dealt with by the fiscal authorities of second instance (provincial financial authorities) — *i.e.*, by the appeal committees attached to these authorities. As stated above, these proceedings relate only to the general profits, income and property tax. The methods of appointing these committees are those applicable to the assessment committees. The taxpayer may, within sixty days, appeal from the decision of the committees to the administrative tribunal, whose jurisdiction extends to the whole Confederation. Such an appeal lies only on the ground of a wrong application of the law, or some material fault of procedure.

Taxes are collected as follows :

(a) *By Direct Payment* in accordance with the assessment notice :

- (1) As regards the general profits and company taxes, in all cases ;
- (2) In the case of the income-tax and the taxes on salaries and capital yield, when the tax has not already been deducted at the source.

(b) *By withholding at the Source.* — Deduction must be made by those from whom the taxpayer is entitled to receive payment of the taxable amount. They have to calculate the tax, withhold the tax due on each occasion of payment and pay it into the Treasury at stated times.

This method applies :

- (1) As regards tax on directors' percentages, to all cases ;
- (2) In connection with income-tax, and taxes on salaries and capital yield (only in certain cases). As regards the two former, the method applies to wages and salaries ; as regards the last, it applies to interest on securities, bonds, savings-bank deposits and current accounts).

When, notwithstanding deduction at the source, it is found that official assessment is necessary, allowance is, of course, made for tax previously collected.

PART II. — METHODS OF TAXING FOREIGN AND NATIONAL ENTERPRISES.

A. FOREIGN ENTERPRISES.

I. DEFINITION AND GENERAL PRINCIPLES.

The term "foreign enterprise", although familiar in Austrian legal terminology, is nowhere expressly defined. As regards enterprises run by individuals or by associations of persons having no distinct legal entity, the Law on Personal Taxation (paragraphs 5, 83, 90 and 153) permits considering such enterprises as foreign which either operate exclusively through an establishment situated abroad or extend their operations *into* Austria *from* an establishment situated abroad, or, in the absence of headquarters of this sort, from a foreign seat of domicile of the owner of the enterprise (*Unternehmer*). In practice, this interpretation is adopted by the fiscal authorities. In the case of companies with a distinct legal entity, such companies are foreign when they have been established abroad in accordance with foreign laws.

As regards the principles governing the taxation of foreign enterprises, a distinction must be made between the two following cases :

(a) Enterprises exercising activities productive of income in Austria.

In such case the basic principle is that foreign enterprises having a permanent establishment in Austria are taxable to the extent of their industrial and commercial activities in Austria. From the fiscal standpoint, it matters little whether or not the Austrian establishment owned by a foreigner itself receives the proceeds of its operations or not.

Furthermore, foreign owners of enterprises are taxable in Austria when, without having an establishment in that country, they pursue their industrial or commercial activities through various methods of exploitation or through commercial travellers, or, lastly, through their own personal activities. (Of course, the last case cannot apply to companies with a distinct legal entity.) In all these cases, the Austrian tax is imposed on the fruits of activities pursued in Austria. There is one further case where the income of a foreign enterprise is liable to Austrian income-tax, even where such enterprise does not operate in Austria — viz., where the owner of a foreign enterprise is domiciled in Austria.

There is no exact legal definition of a "permanent establishment". The only permanent establishments specifically mentioned are branches, factories, and buying and selling offices ; it is, however, added that the existence of a permanent establishment may also ensue from other circumstances. There are numerous judgments of the Austrian Administrative Tribunal dealing with the definition of a "permanent establishment". To create an "establishment" (*Betriebsstätte*), it is sufficient that there should exist in Austria an organisation (*Einrichtung*) controlled by the owner or employees of a foreign enterprise (Official Collection of Judgments of the Administrative Tribunal No. 11717, 1918). Such organisation need, moreover, only be auxiliary (*Hilfseinrichtung*) (ibid. 13481, 1925). The establishment need not have its own

independent revenue (ibid. 10844, 1925). Nor is it necessary that it shall be engaged in specifically industrial or commercial work ; information bureaux (ibid. 9554, 1914), technical offices (ibid. 7238, 1909), offices in charge of foreign accounts (ibid. 13481, 1925) count as branches (*Niederlassungen*) ; so does a goods depot in Austria (ibid. 11951, 1918). A foreign enterprise permanently represented in Austria by an agent residing in that country may also be regarded as having an establishment there (ibid. 12592, 1921) (see also pages 23-24).

Profits earned in Austria are liable to the profits taxes — *i.e.*, either the tax on general profits or the company-tax in the case of Austrian enterprises owned by foreign companies liable to this particular form of tax on profits. Where the foreign owner is an individual, he is further liable to income-tax on income derived from his activities in Austria. Where a foreign concern is a partnership, each partner is taxable in respect of his share of the profits from activities in Austria. If these partners are individuals, they pay income-tax ; if they are commercial companies having legal entity, they pay the company-tax (cf. page 12). However, foreign partners which merely possess holdings represented by shares or similar securities in Austrian enterprises are not subject to income-tax or to the company-tax.

(b) Even in the absence of the aforementioned conditions whereby foreign enterprises are assessed on their profits, these enterprises, like all foreigners, are taxable in respect of certain income accruing to them from Austria — *viz.*, income from landed property and buildings, or from directors' percentages or royalties from property rights in Austria (for details see Section 2 below).

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) *Dividends.*

Dividends accruing to foreigners from Austrian securities are taxable in Austria only in so far as they form an integral part of commercial or industrial income taxable in Austria and realised by an Austrian establishment of the foreign concern, or if the foreigner drawing these Austrian dividends is domiciled in Austria and thereby liable to income-tax. Dividends are never taxed at the source.

(b) *Interest.*

(1) *On Bonds.* — Where the interest is on bonds issued by share companies, the tax on them is included in the tax payable by the company which pays the interest. Foreign enterprises in receipt of such interest are therefore not taxable in respect thereof, except where the interest is an integral part of income taxable in Austria and earned by the Austrian establishment of that foreign concern. Interest on bonds issued by public corporations is liable to the tax on capital yield which is collected at the source. Once again, income-tax is payable in the case of interest on bonds, when a foreigner is domiciled in Austria.

(2) *On Secured Loans.* — Interest from debts secured by mortgages is subject to the tax which is levied on industrial or commercial revenue earned in Austria where such interest is a constituent part of the taxable income of the Austrian establishment of a foreign concern. Otherwise, such interest is liable to the tax on capital yield which is collected on the basis of the creditor's return, and, where the latter is an individual, such interest is liable to income-tax regardless of whether he is or is not domiciled in Austria.

(3) *On Unsecured Loans.* — Similarly, where interest accrues from loans other than those mentioned under (1) and (2) above and forms a constituent part of commercial or industrial income taxable in Austria, such interest is also taxable. Otherwise, the creditor is liable to the tax on unearned income in accordance with a return he is bound to make. Where, however, the person to whom the interest accrues is not domiciled in Austria, he is not liable to income-tax.

Interest on current accounts is not subject to the above method of taxation when paid by credit institutions and banks. In this case, the statutory tax on capital yield has already been deducted at the source. Exemption, however, is granted to interest of this class on money imported from abroad in the form of foreign currency. This exemption is, however, only temporary.

(c) *Directors' Percentages.*

Directors' percentages are liable in Austria to a special tax, which is deducted at the source, and, further, to income-tax on the basis of the recipient's declaration, regardless of the latter's domicile. In practice, only individuals are in receipt of these percentages. Austrian share companies are required to deduct this tax at the source from the full amount of the percentages paid by them to their directors, even where the company owns foreign establishments the income from which is not assessed to tax in Austria. The courts do not take into account that these percentages may have been partly paid out of the income from foreign branches (Official Collection of Judgments of the Administrative Tribunal, No. 10834, 1925).

(d) *Royalties for Use of Patents, Copyrights, Trade-marks, Secret Processes and Formulæ and Similar Income.*

This income is taxable in Austria when the person concerned has set up an establishment in the country with a view to exploiting his rights there, or when, in the absence of such establishment, he is domiciled in Austria. Where the owner of an enterprise is domiciled abroad, but exploits his rights in Austria without setting up an establishment there for that purpose, he is not taxable. However, where the remuneration received by the foreigner concerned in payment of his exploited rights is such as to constitute participation in an Austrian enterprise, such remuneration is treated as part of the taxable income of the Austrian enterprise, so that the foreign beneficiary is himself liable like any other foreign partner.

(e) *Rents from Real Estate, Mining Royalties and Similar Income.*

All income from land and buildings is essentially taxable in Austria. When such income constitutes an integral part of the total income of the Austrian establishment of a foreign company or partnership, it is included under the tax which is levied on industrial or commercial income earned in Austria. Where income from landed property and buildings is earned apart from any such establishment, it is taxable *per se*. Where the income accrues to individuals, it is liable to income-tax; where it accrues to companies possessed of a legal entity, it is liable to the company-tax. Further, income of this sort is liable in the provinces to various local taxes on land and buildings.

(f) *Gain derived from the Purchase and Sale of Real Estate, Securities and Personal Property.*

Profits accruing to individuals and to partnerships which are liable to the general tax on profits from sales of this kind, when such sales are normal transactions of an enterprise operating for profit or are speculative transactions, are taxable in Austria regardless of the nature of the thing sold. The Administrative Tribunal has, however, ruled that not every alienation of property forming part of the assets of an enterprise of necessity constitutes such a normal transaction. The test is whether the sale in question corresponds with the nature and true purpose of the enterprise (Official Collection of Judgments of the Administrative Tribunal, No. 12133, 1919, etc.). Thus, the mere fact that certain real property has figured in the books of an enterprise raises no presumption that the alienation of such property is a normal trading transaction (*ibid.* 12448, 1920). In the case of companies liable to the company-tax, the system is different, for the tax is imposed

on all profits from the sale of any property accruing to the Austrian branch of a foreign enterprise. In accordance with the structure of this tax, profits from sales of this sort always form part of the surplus balance in the accounts upon which the tax is levied. The motive and purpose of the sale are of no account.

(g) *Salaries, Wages, Commissions and Other Remuneration for Services.*

Income of this sort earned in Austria fulfils the legal requirements for liability to the tax on salaries, which is deducted at the source. It is also liable to income-tax, even when the recipient is domiciled abroad. As regards directors' percentages tax, see (c) above.

(h) *Income from a Trust.*

Fiduciary administration of capital in the shape of a trust is not known to Austrian law. Individuals resident in Austria in receipt of income from foreign trusts of this sort are treated as if the income came to them direct.

(i) *Income from the Carrying-on of a Business or Industry through :*

(1) *A Local Commission Agent or Broker.* — Commission agents and brokers operate in their own names on behalf of their principals. Austrian law and jurisprudence do not regard the relations between the owner of a foreign concern and the commission agent or broker in Austria as constituting an establishment of the foreign enterprise. The independent operations of the commission agent or broker do not constitute an extension of foreign operations to Austria. They are looked upon as independent Austrian activities on the part of an Austrian business man, even if in the last analysis the effect of the latter's operations is to enable the foreign trader to market goods or conclude a deal. This principle also applies where the Austrian commission agent holds, subject to a subsequent settlement of accounts or return of the goods, stock belonging to the foreign trader, which he disposes of in his own name.

The foreign enterprise is not, in these circumstances, taxable.

On the other hand, the fiscal authorities treat business relations as implying the existence of an Austrian establishment if the Austrian agent is in a position of complete financial dependence upon his foreign principal — that is to say, when the latter's control over the former's activities is so complete that the commission agent, although theoretically independent, is, in fact, an executive organ of his foreign principal and thus discharges the duties of an employee. In such a case, the foreign enterprise is taxed in Austria.

(2) *A Local Dealer or Distributor.* — Where an independent Austrian business man purchases on his own account, for resale, goods from a foreign enterprise (*i.e.*, does not sell simply on commission as in paragraph 1), *a fortiori* there is no taxation of the sort discussed in paragraph 1. Equally, the tax does not apply where the foreign trader undertakes not to supply his goods to any other Austrian merchant for resale.

(3) *A Travelling Salesman, whether or not having Power to conclude a Contract.* — The employment of commercial travellers in Austria does not imply the existence in that country of an establishment within the terms of fiscal law, but it does represent an extension of business to Austria and, as such, it is liable to Austrian tax. Fiscally speaking, this very loose form of business extension to another country has many drawbacks. First, it is hard for the revenue authorities to make a suitable assessment of tax, and, secondly, the owner of a business finds the tax extremely burdensome and annoying, since it hits him at a time when he is often unable to foresee the results of his transactions. The Austrian administration has realised the urgent necessity for removing some of the fiscal prohibitions in this sphere by means of treaties with other countries. Austria has worked hard to this end, as will be seen below, (page 24).

(4) *A Local Agent with a Power of Attorney.* — A local agent with power of attorney directly engages the owner of a foreign enterprise and transacts the latter's affairs in Austria. Business transactions of this sort therefore imply an extension of the foreign enterprise to Austria and are taxable as such. Where such a relation is permanent and not merely occasional, the operations of the agent constitute an establishment belonging to the owner of the foreign enterprise.

(5) *An Agent selling out of a Stock belonging to the Foreign Enterprise.* — The case treated here differs from that in paragraph 1, in that the representative is not a commission agent disposing of goods in his own name, but one who handles stock which is at the disposal of its foreign owner. Business relations of this class are treated by the law as an Austrian extension of the foreign concern falling under the head of "methods of exploitation" in Austria, and are, as such, taxable. Where the relation is a permanent one, it falls under the definition of an Austrian goods depot and constitutes an establishment within the meaning of Austrian fiscal regulations.

(6) *A Permanent Establishment of any Kind.* — Attention has already been drawn to the circumstances in which the operations of agents in Austria imply the existence of establishments belonging to the owners of foreign enterprises. Further, every permanent organisation owned by a foreigner constitutes an Austrian establishment and is accordingly, under Austrian law, taxable to the extent of the income accruing therefrom. For an explanation of the term "establishment", see above, pages 20 and 21. In Part III of this study, details will be given concerning the practical application of the tax.

3. TREATY PROVISIONS.

International treaties embody notable qualifications of Austrian fiscal law, as mentioned above. These treaties restrict liability to taxation to cases where owners of foreign enterprises have set up establishments in Austria. The treaties do not always adopt the same definition of the term "establishment", but, on the whole, the definition corresponds roughly to that formulated on pages 20 and 21. They forbid Austrian taxation in all cases where, following ordinary Austrian legislation, it does not rest on the existence of a permanent establishment but where the use of "methods of exploitation" or the temporary deployment of activities in Austria through employees or agents is alone ground for liability. On page 23, care was taken to indicate the conditions in which the employment of agents is deemed to constitute an establishment. The scope of the treaty restrictions should thus be quite intelligible. Under these provisions, taxation is altogether forbidden in cases falling within No. 3, page 23; it is forbidden in cases falling within Nos. 4 and 5, above, where the business relations concerned are not of a permanent nature. The taxation of commercial travellers' activities, which is felt to be especially vexatious in its effects, is mitigated, not only under the fiscal treaties, but also under numerous commercial treaties¹ concluded by Austria. Whereas, however, the fiscal treaties aim at abolishing altogether the taxation of income derived from the employment of commercial travellers, the commercial treaties are restricted to excluding from taxation certain specific activities of commercial travellers. These treaties deal only with certain cases: those where the foreign *entrepreneur* does not own an establishment in Austria but, through authorised commercial travellers in his employ, purchases goods from merchants or in the open market or from persons producing these goods, or, secondly, takes orders (even carrying with them samples) from tradesmen or other persons dealing professionally in the class of goods concerned. Even where no commercial treaties of this kind exist with foreign countries, the Austrian Government has gone so far as to remit the tax to the same extent as provided for in treaties with other Powers, provided that the foreign countries concerned grant Austria reciprocity of treatment in this respect (Decree of April 10th, 1924, by the Federal Ministry of Finance, B.G.Bl., No. III).

¹ A complete account of the relevant commercial treaty provisions will be found in GOTTLIEB-BILLROTH-EGGER, *Personalsteuergesetz*, Volume II.

The fiscal treaties also provide for fiscal alleviation in the case of certain forms of income which are taxable independently of the fact that they belong to the enterprise. Thus Austria remits the tax on interest from certain loans mentioned on pages 21 and 22. In such cases the tax is only levied where it is deducted at the source, while some agreements also retain the tax on income from mortgage loans. The treaties with Germany and Switzerland, however, make the domicile of the creditor the test even for taxation of income from mortgage loans. Further, the payments of salaries and wages, when made to an individual living abroad, are tax-free in Austria (with the exception of monies paid out of Austrian public funds).

B. NATIONAL ENTERPRISES.

I. DEFINITION AND GENERAL PRINCIPLES.

There is no express legal definition of the term "national enterprise". The expression includes all enterprises directed *from* an establishment situated in Austria, or, in the absence of such establishment, from a place of domicile situated in that country. Companies having their head office in Austria are regarded as national enterprises and, as such, taxable. The notion of "real centre of management" is unknown to Austrian law. There is, however, no doubt that such a centre is to be considered a permanent organisation liable to Austrian taxation. From the fiscal standpoint, such a centre would, generally speaking, play the part of the statutory seat, which, in the normal course of events, is identical therewith.

National enterprises are normally taxable on the whole of their trading results. An exception is, however, made in the case of a national enterprise having a permanent establishment abroad. The term "establishment" bears the same meaning as in the case described on pages 20 and 21. Here income from foreign trading is tax-free, if already taxed abroad. Further, in the case of enterprises liable to the general tax on profits, the fiscal authorities require that the foreign tax shall be similar to the Austrian tax, and that the foreign country concerned shall accord reciprocity of treatment. But in the case of companies liable to the company-tax, the law does not require close enquiry into the nature of the foreign tax nor does it demand reciprocity. Nevertheless, it prescribes that, in any event, a certain minimum of the total income shall be liable to Austrian tax. In the case of enterprises liable to the general tax on profits, this minimum is a quarter of the total income. In the case of companies liable to the company-tax, it is one-tenth. In assessing income from foreign trading, the company-tax also makes provision for certain maxima. This in two cases: in the case of goods exported to Austria from abroad, or *vice versa*, the foreign revenue may not exceed one-half of the total revenue from the business in question. In the case of goods manufactured in Austria and sold abroad, the foreign income may not exceed one-third of the total income from such activities.

In calculating these deductible amounts, the revenue authorities may require access to all books, documents, etc.; more especially, they may require the production of the foreign establishment's separate accounts.

2. TAXATION OF CERTAIN KINDS OF INCOME.

The general principle outlined in the preceding section makes further explanation superfluous.

3. TREATY PROVISIONS.

Fiscal treaties deal also with the taxation of national enterprises. Foreign establishments belonging to Austrian nationals are exempt from taxation without the enquiry into the foreign fiscal system which would otherwise be required by law. Further, income from foreign landed property and, under several Conventions, even mortgage interest is exempt from Austrian taxation.

Finally, interest on capital taxed abroad by deduction at the source is free from Austrian tax on capital yield. This provision is, however, qualified. Within certain limits, income of this sort may remain subject to Austrian tax as constituting the result of operations for profit conducted in Austria (for instance, mortgage interest from abroad accruing to an Austrian mortgage bank). From this it appears that, in spite of the treaties, there is still a certain conflict between the two fiscal systems. In such cases, the difficulty is due to the fact that we are confronted with two fundamental principles diametrically opposed to each other — the taxation, at the seat of the enterprise, of commercial and industrial profits realised without any foreign establishment and including income from real property regarded as a constituent part of the whole income of the enterprise, and the taxation of the same income from real property in the country where that property is situated.

PART III. — METHODS OF ALLOCATING TAXABLE INCOME.

A. FOREIGN ENTERPRISES WITH LOCAL BRANCHES OR SUBSIDIARIES.

I. GENERAL QUESTIONS AND METHODS OF APPORTIONMENT.

(a) BOOK-KEEPING AND ACCOUNTING REQUIREMENTS.

According to Austrian commercial law, every trader carrying on business in Austria has to keep books (Law of December 17th, 1862, *Imperial Law Gazette*, No. 1 of 1863 and Amendment to Commercial Law of February 16th, 1928, *Federal Law Gazette*, No. 63). This obligation also extends to business enterprises whose operations are of a character and extent that necessitate commercial organisation. Exemption from the obligation is granted only to persons whose commercial operations do not exceed the bounds of petty trade. The legislative provisions concerning book-keeping (Articles 28 to 36 of the Commercial Law) require that traders shall draw up an annual inventory and balance-sheet. Foreign owners of enterprises must, of course, likewise comply with these requirements whenever they organise branches in Austria with a view to extending their commercial and industrial business to that country.

Foreign share companies (*Aktiengesellschaften*) authorised to engage in trade or industry in Austria must submit to the Austrian authorities every year the general balance-sheet for the company, the separate balance-sheet of the Austrian establishment and the minutes of general meetings (Imperial Decree of November 29th, 1875, *Imperial Law Gazette*, No. 127). The special balance-sheet relating to the Austrian establishment of share companies must show the assets assigned to that establishment and the plant situated in Austria separately from the rest of the company's property. Limited liability companies (*Gesellschaften mit beschränkter Haftung*) are required to keep separate regulation books for their Austrian operations (Article 112 of the Law of March 6th, 1906, *Imperial Law Gazette*, No. 58). Lastly, banks with limited liability (*Bankgesellschaften mit beschränkter Haftung*) are required to publish their Austrian balance-sheet and the balance-sheet of the chief foreign establishment.

(b) METHODS OF ALLOCATION.

Austrian fiscal law contains no special provisions specifying how to determine the income to be ascribed to the Austrian establishment of a foreign enterprise; the rules applicable to the Austrian establishment have to be deduced from the general provisions for determining the basis on which profit-seeking enterprises are assessable. These general provisions show that, although first consideration has to be given to the separate accounts of the Austrian establishment and its statements of profit and loss, these data are not of themselves enough, and recourse must be had

to estimates. These may not only be based upon certain indices suggested by experience and directly associated with obvious outward signs of the activities exercised in Austria, but may also be framed by a fractional determination based upon the total profits of the enterprise. The series of operations in detail is as follows :

1. *Method of Separate Accounting.*

Experience has shown that all foreign enterprises which set up establishments in Austria are on a scale exceeding the limits of petty trade. (We may disregard economic relations within the frontier zones as being outside the sphere of our enquiry.) For our present purpose, therefore, we are concerned with enterprises subject to the accountancy obligations set forth under (a) above.

Accordingly, when an establishment complies with this obligation, it is in a position to keep separate accounts showing the results of its Austrian operations. In practice, however, it is not, in most cases, possible to rest content with the particulars of the separate balance-sheet, since the relations between the Austrian and foreign establishments of a single enterprise offer a very wide field for the deliberate distortion of facts in the accounts.

Thus, in particular, it is possible to invoice at more or less arbitrary prices either goods coming from the manufacturing establishment abroad and imported into Austria to be sold there or goods supplied by Austria to the foreign establishment for sale abroad ; in this way, it becomes easy to transfer the commercial profit realised in whatever way may be thought best. It is certainly not in accordance with the fundamental principles of fiscal law that the Administration should be bound by book entries of this kind. It has therefore the right to resort to any available methods of framing estimates in accordance with real facts and to substitute its own figures for those of the owner of the business. The exercise of this right is not confined to the case of a branch dependent on the foreign owner, but extends to any taxable enterprise in Austria possessing a distinct legal entity when that enterprise is economically dependent on another enterprise or is identical with the latter, and when the results of its operations are distorted by a false statement of prices, purchases from the other enterprise being entered at too high a price or sales at too low a figure.

This case may also arise when an Austrian company is legally independent but is economically completely under the control of the foreign parent company for the reason that the latter holds the majority of the shares of the subsidiary. Even in the case of purely Austrian transactions, the fiscal authorities may undertake corrections of this kind ; in the case, for example, of deliveries between a company by shares and one of its big shareholders or between several associates bound to each other by the possession of shares in each other's enterprises. Several judgments of the administrative tribunal have recognised the legality of this right to make corrections (*e.g.*, Official Collection of Judgments of the Administrative Tribunal, Nos. 13565, 1925 ; 14614, 1928 ; 14146, 1927 ; 8367, 1911 ; etc.).

From the viewpoint of fiscal procedure, corrections of this kind are mainly a cause of difficulty. Delivery prices are ordinarily checked by comparison with the prices paid to or asked by Austrian enterprises of the same kind or by comparison with official price lists, or by enquiries on the part of experts. Price corrections of this kind are, however, not the only way of departing from the separate accounts submitted by the enterprise. Other receipts may be wrongly shown in the accounts in favour of the foreign centre of management of the enterprise, and may represent the transfer of business results which ought really to be ascribed to the Austrian concern. Such transfers may occur in the following cases : the attribution in the accounts of interest resulting from a more or less artificial allocation of the capital endowment allotted to the establishment by the centre of management ; the attribution of emoluments in recognition of the services of foreign directors ; the attribution of royalties for the sale of patents and similar rights exploited in manufacturing operations. These artificial allocations to the centre of management must always be regarded as part of the results of operations in Austria, and the Treasury must therefore include them for purposes of Austrian tax and correct the separate Austrian accounts.

2. *Empirical Methods.*

The method described under 1 often has very unsatisfactory results, particularly when the activities of the Austrian establishment do not constitute a compact whole, but are either auxiliary and subordinate operations or are only one stage in a plan of operations carried out by the foreign enterprise. In such cases, the profits shown in the separate balance-sheet are most often calculated on the basis of arbitrary estimates drawn up by the owner of the enterprise.

In order, therefore, to satisfy the law, the Administration has to determine the results of the operations transacted in Austria. For this purpose, recourse is generally had to certain indices furnished by experience and bearing upon certain outward signs revealed by the enterprise. Of these, the most important is the Austrian turnover. The law contains no provisions fixing a general percentage of turnover to represent the taxable profits. It rests with the authorities to arrive at a fair estimate by a comparison with the results of other similar enterprises taxable on the basis of regular accounts. It is the practice of the fiscal authorities, whenever possible, to fix the index by friendly agreement with the taxpayer and thus allow the latter to make arrangements to avoid simultaneous taxation in Austria and abroad.

3. *Method of Fractional Apportionment.*

If, owing to the impossibility of applying the method referred to under 1, the Administration has to resort to estimates, there is nothing, in principle, to prevent the authorities from framing their estimate on the basis of an apportionment of the enterprise's total profits. In most cases, however, the procedure does not furnish satisfactory results, because it necessitates first determining those profits, which is a very difficult matter.

In determining the basis of assessment, the Administration is not confined simply to demanding the accounts of the Austrian establishment ; if these are not considered sufficient, it may ask for general information relating to the whole enterprise. Unfortunately, taxpayers are often unable to furnish the information asked for, because its sources are to be found abroad. The information is accordingly beyond the direct reach of the fiscal authorities ; in particular, the authorities are unable to inspect the accounts — an essential matter when it is a case of calculating tax on the basis of commercial books.

In the case of Austrian establishments subject to company-tax, the Austrian law contains a subsidiary provision akin to the fractional method we are discussing (section 90, paragraph 3 of the Law on Personal Taxation). The law provides, as the minimum taxable in Austria, a fraction of the profits due to the *joint activity* (*gemeinsame Tätigkeit*) of the Austrian establishment and the foreign centre of management (not therefore the *total* profit of the foreign enterprise). We give below (pages 32 and 33) further details concerning the fractions laid down for the different kinds of business relations. Owing to the above-mentioned difficulty of ascertaining the total profit of the foreign centre of management and, in particular, the share of this profit representing the joint activity of the enterprise and its establishment, the importance of this provision in the law is more theoretical than practical.

This method of apportioning income in accordance with certain fractions is adopted in the special Conventions concluded by Austria with Czechoslovakia and Hungary. The main features of these Conventions, the details of which will be frequently referred to in this study, are as follows :

The fiscal authorities disregard the separate balance-sheets of establishments. They take the total profits of the enterprise and fix the joint profits from some obvious outward index — viz., the turnover of the joint operations conducted by the enterprise and its establishment. They then allocate these profits according to certain indices laid down by the Conventions. While these indices coincide numerically with the taxable minima mentioned above and referred to later (on pages 32 and 33), they represent an essentially different method of settlement. In fixing minima, the law is only furnishing the authorities with a standard by which to correct the profits as shown

in the separate accounts. The Conventions, on the other hand, lay down the scale of fractions as a rule to be applied automatically and without reference to the separate accounts.

4. *Requirements for Selection of Methods and Value of the Various Methods.*

The Administration cannot refuse to assess tax on the basis of the separate accounts submitted to it, unless it can first show that this method is unable to furnish any practical result. This happens, unfortunately, only too often, but it is only then that the fiscal authorities may have recourse to other methods.

Theoretically, the method of separate accounts would be perfectly satisfactory, if only these accounts gave a true picture of the results of operations in Austria. In many cases, however, experience shows that these accounts are submitted in such an arbitrary form that the whole method loses much of its value. The other methods may, as a rule, satisfy the fiscal requirements of the State in which the separate establishment is situated, but the soundest method for the States which are collecting the tax is undoubtedly that of a fractional apportionment of total profits. Nevertheless, all these methods aggravate the risk of double taxation in Austria and abroad, and they are only satisfactory when the indices of apportionment are selected by agreement between the two countries between which the tax is to be divided. This is the plan provided in the Conventions concluded by Austria with Czechoslovakia and Hungary (see below).

(c) APPORTIONMENT BETWEEN BRANCH AND PARENT ENTERPRISE.

1. *Apportionment of Gross Profits of Local Branch to Real Centre of Management abroad.*

When the profits accruing to the Austrian establishment have been determined by one of the above-mentioned methods, there is no further occasion to allocate these profits between the Austrian establishment and the centre of management abroad. Accordingly, the fiscal authorities do not recognise any so-called "*Sitzquote*" representing the proportion of the profit to be ascribed to the centre of management abroad.

This principle also applies under the fiscal regime of the Conventions, the only exception being the agreement with Hungary. Under that agreement, and in the case of enterprises liable to the company-tax, the tax is levied on a minimum fraction of the total profit (one-tenth) in favour of the State in which the enterprise is situated. For the taxation of an Austrian enterprise with an establishment abroad, the law lays down a minimum percentage to be ascribed to the seat (see page 35).

2. *Apportionment of Expenses of Real Centre of Management to Branch.*

Interest Charges. — When an undertaking has contracted a debt against the issue of bonds and debentures, it is not required, for purposes of Austrian tax, to allocate certain parts of this debt between the central seat and the branch, since the law does not, in principle, allow the debtor concern to deduct from the taxable amount interest on bonds. In other words, the law taxes this form of interest by taxing the debtor company at the source. It does not, in this respect, treat share capital differently from debenture capital, and therefore contains no rules for allocating these debenture debts to the different establishments.

In regard to other debts — for instance, short-term bank debts, interest on which the law allows to be deducted when taxing the enterprise which pays it — the fiscal authorities take account of the whole or part of this interest service when taxing the branch. This deduction is allowed only if it is shown that the debt in question was contracted on behalf of the branch and actually applied to it. The law contains no provision for the general allocation of these debts on the basis of outward signs, but, in case of doubt, the relation between the two turnovers may at any rate serve as a guide.

General Overhead. — When a foreign enterprise has an establishment in Austria and enters certain expenses affecting the whole concern exclusively to the seat of management abroad, it is not, in principle, forbidden to deduct from the amount taxable in Austria the share of these expenses, which, in fact, belongs to the Austrian establishment. The Administration checks the accuracy of the percentage deducted by the Austrian establishment, taking account for the purpose of actual circumstances. In such cases, this operation generally consists of estimating the reasonable character of the sum mentioned. Frequently, the Administration calculates the Austrian share of the total expenses on the basis of the relation between the turnover of the Austrian establishment and the total turnover of the enterprise.

3. *Apportionment of Net Profits.*

Whether it is a question of the apportionment of the net profits of the branch to the deficitary parent or, on the contrary, of a part of the profits of the parent to the deficitary branch, account should be taken of the method by which the Administration applies the tax.

If the tax is calculated for the branch separately on the basis of its results as shown in its separate accounts, the figure thus arrived at, whether a profit or a loss, is not affected by the total results of the parent enterprise abroad. If, therefore, this method of determination shows a profit to the branch, it will not affect the basis of assessment if it turns out that the parent enterprise abroad closed its accounts with a total loss after balancing the Austrian profits against losses sustained by other establishments. On the other hand, if the separate accounts reveal a loss on Austrian operations, any profits of the whole enterprise resulting from successful operations elsewhere will not be subject to Austrian tax.

If, however, Austrian tax is levied, not on the basis of separate accounting, but according to the method of fractional apportionment, that tax will depend on the total results for the whole enterprise. In this case, therefore, the general result will be indirectly subject to Austrian taxation to a proportionate extent.

These repercussions of the results of one branch upon the taxation of other branches are especially felt under the above-mentioned system of allocation established by the special agreements between Austria on the one hand, and Czechoslovakia and Hungary on the other.

(d) APPORTIONMENT BETWEEN PARENT ENTERPRISE AND SUBSIDIARIES.

A subsidiary, by virtue of its legal structure, must be regarded as a legally independent organism. Its internal relations with the foreign company upon which it depends or by which it is controlled, for the reason that the foreign company holds its shares, do not of themselves render the foreign company liable to taxation. These relations do not make the subsidiary an establishment of the foreign parent. They do, however, influence the taxation of the Austrian subsidiary in the same way as a similar relationship between two Austrian companies may influence the taxation of both of them. This occurs particularly when two mutually dependent companies supply each other with goods at prices which the Treasury deems to be entered incorrectly. The authorities then find it necessary to alter these prices so as to apply the tax as if the transactions in question had been between two independent parties. (On this point see the observations made on page 28.)

This alteration presupposes the adjustment of the prices calculated by the company and is made by a process of checking, in which the company, unless it is in liquidation, may participate by submitting proposals. The alterations are based on a comparison with the information furnished by other similar enterprises, on existing market prices and, in the absence of such evidence, on expert opinion. The experts consulted are usually traders in the same or similar branches of business, but excluding competitors or persons directly participating in the enterprise. Nevertheless, corrections of this kind in the taxation of subsidiaries do not involve the taxation of the foreign parent. There may, of course, exist relations between the two companies, according to the nature

of the operations by the subsidiary, which would make the latter an establishment of the foreign parent, just as an individual may be the employee or agent of a foreign enterprise exercising functions equivalent to those of an establishment of that enterprise. This case was dealt with in Part II of the present study. In such circumstances, the business relations between subsidiary and parent constitute grounds for taxing the latter, and compel the fiscal authorities to determine what share of profits is to be ascribed to the foreign parent. This is done exactly as was described above in the case of establishments having no distinct legal entity.

II. APPLICATION OF THE METHODS OF ALLOCATION IN SPECIFIC CASES.

(a) INDUSTRIAL AND COMMERCIAL ENTERPRISES.

The Austrian law contains no precise rules for applying the principles set forth above to the different kinds of business relations, except in the case of enterprises liable to the company-tax. In their cases, it ascribes to Austria a taxable minimum of the joint profits. As pointed out on page 23, this provision of the law is of limited practical importance. It is only a subsidiary rule and, in order to calculate the tax, the Administration must, in principle, have regard to the separate accounts of the establishment; however, it furnishes the Administration with some guidance when it comes to correct the receipts as shown by the separate accounts. In certain cases, where the activities of the enterprise extend to several countries, the yield of the Austrian establishment must not be less than a certain fraction of the receipts from the joint operations in Austria and in the country in which the main enterprise is situated. The different fractions to be applied according to the nature of the operation are given below. The application of this rule assumes that the profits from the joint operations of the Austrian branch and the foreign parent are deducted from the latter's total profit, for this is, as a rule, not confined to business transactions with the Austrian branch. In practice (see page 29), this operation often breaks down owing to the difficulty of determining the amount taxable, for the fractions indicated as minimum limits in this case cannot be directly calculated by reference to the total profits of the foreign enterprise. The only way of fixing them is to base them on the share of total profits represented by transactions with the Austrian establishment.

In regard to the general cases we have been considering, these minimum fractions constitute nothing more than a subsidiary rule. Under the special Conventions with Czechoslovakia and Hungary, however, they constitute a general principle of universal application. They are, moreover, associated with a rule for determining the share in the total profits of the enterprise which appertains to transactions between the Austrian establishment and the parent enterprise abroad; and it is this rule which makes this clause in the treaties really effective. The other fiscal Conventions make no provision for minimum quotas, but retain the method of calculation based upon separate accounts.

The rule of minimum quotas only concerns certain particularly common cases of business extensions to Austria. It is, however, far from providing a complete solution to the question. Accordingly, the Administration has, apart from the law, devised certain methods of procedure which it applies to the treatment of enterprises operating in several countries.

Details are as follows:

I. *Selling Establishments.*

Local Establishments selling in National Market. — When a foreign manufacturer sells through an Austrian establishment goods which he has manufactured abroad, the law provides that at least one-third of the profits from these joint operations shall be liable to Austrian tax. When, however, a dealer, through his Austrian establishment, sells in Austria goods which he has bought abroad, the Austrian Treasury claims tax on at least one-half of the joint profits. The rule shows that, in such cases, Austrian law does not limit the amount taxable in Austria to the difference between the

wholesale and retail price, but considers a part of the total profit as the share belonging to the Austrian establishment.

The same fractions apply under the special agreements with Czechoslovakia and Hungary, not, however, as minimum quotas, but as the general rule.

Local Establishments of Foreign Enterprises selling abroad. — When the local selling establishment extends its operations to third countries — that is to say, when the business transacted in these third countries is conducted by the local establishment — these operations are taxable against the establishment.

2. *Manufacturing Establishments.*

When an enterprise manufactures in Austria and sells abroad, the law prescribes that at least two-thirds of the joint profit is to be ascribed to the Austrian manufacturing establishment.

The same fractions — representing the general rule and not minimum quotas — apply under the special agreements with Czechoslovakia and Hungary.

3. *Processing Establishments.*

An estimate has to be made of the share of profits corresponding to the activities of these processing establishments, but the law has no special rules in regard to them. Nor has experience evolved any generally applicable principles. The necessary determination may, however, be considerably facilitated by a comparison between the labour costs of the processing operations in Austria and the total costs of production. Even the special agreements with Czechoslovakia and Hungary contain no ruling on this point.

4. *Buying Establishments.*

When the owner of a business purchases Austrian goods through his Austrian establishment with a view to selling them abroad at least, half the joint commercial profit is, as in the case quoted under 1, ascribed to the Austrian buying establishment. The same fractions apply under the Austrian Conventions with Czechoslovakia and Hungary, not, however, as minimum quotas, but as the general rule.

Establishments for the purchase of raw materials for manufacture abroad are subject to tax, but the law makes no special provision in this connection. The separate agreements with Czechoslovakia and Hungary make no mention of these establishments, but they contain a clause to the effect that the usual commission on business of this kind must be ascribed to the detached establishment.

5. *Research or Statistical Establishments, Display Rooms, etc.*

These establishments also are subject to taxation in Austria. There are no special provisions for determining the basis of assessment. The importance of an establishment of this kind may vary within very wide limits; an office which appears to be a mere information bureau (*Ueberwachungsstelle*) may in reality conceal the seat of management. Normally, however, such establishments perform purely auxiliary functions, and the amount on which tax will be assessed must correspond to a fair return for the duties they discharge.

The Czechoslovak and Hungarian agreements do not mention these establishments. The general rule ascribing the usual trade commission as profits of the establishment can often be applied.

(b) BANKING ENTERPRISES.

Here the usual guide is the separate accounts of the enterprise. The interest on loans granted by the Austrian branch must always be counted among the profits of that establishment.

The special agreements with Czechoslovakia and Hungary contain a special rule for credit institutions to the effect that total profits must be apportioned according to the ratio between the costs of personnel (salaries and wages).

(c) INSURANCE ENTERPRISES.

According to the law, these enterprises are taxed on the basis of their separate balance-sheets. The only special provisions on the subject are to be found in the agreements with Czechoslovakia and Hungary, according to which the total profits have to be allocated in proportion to the respective annual net premiums.

(d) TRANSPORT ENTERPRISES.

These enterprises are taxed on the basis of their separate balance-sheets.

Only the agreements with Germany, Czechoslovakia and Hungary contain special provisions.

According to the agreements concluded with Czechoslovakia and Hungary, *railways* shall only be taxed at the place where the enterprise is situated, subject to the latter only operating, in the other State, the part of the line which extends to the first junction station, this distance not to exceed 15 kilometres. When the line covers more than 15 kilometres, it devolves on the Ministries of Finance of the two contracting States to conclude special arrangements. In practice, when it is necessary to apportion income, the fiscal administrations take as a basis the number of kilometric tons transported in each country.

Under the terms of the agreements concluded with the three countries mentioned above, the right of taxation, as far as the *Danube navigation companies* are concerned, belongs exclusively to the State in which the head office of the enterprise is situated.

When other countries are involved and when no separate balance-sheets exist, the fiscal authorities tax the Danube navigation companies in accordance with an apportionment of the total income on the basis of the number of kilometric tons carried.

(e) POWER, LIGHT AND GAS ENTERPRISES.

In so far as apportionment is practicable in the case of such enterprises, the tax authorities apply the general provisions of the law (separate balance-sheets).

(f) TELEGRAPH AND TELEPHONE ENTERPRISES.

The State, in virtue of its sovereign power, reserves to itself the operation of such enterprises. There is therefore no question of their being carried on both in Austria and abroad.

(g) MINING ENTERPRISES.

In so far as apportionment is practicable here, the tax authorities apply the general provisions of the law (separate balance-sheets).

B. NATIONAL ENTERPRISES WITH BRANCHES OR SUBSIDIARIES ABROAD.

I. GENERAL METHODS OF ALLOCATION.

As already mentioned (pages 25 and 26), the taxation of national enterprises with establishments abroad is subject, in the main, to the same rules as the taxation of Austrian establishments of a foreign

enterprise. In order, however, that the profits of a foreign establishment may be immune from taxation in Austria, they must, in the absence of treaty provisions to the contrary, be liable to tax abroad (see above, Part II, B).

The rules mentioned under A pages 27 and seq. in this part of the report, for determining the Austrian share of the joint operations of Austrian and foreign establishments, apply here in exactly the same way. Thus the minimum quota to be ascribed to Austria is half the income from these joint activities in the two following cases : (i) when an Austrian enterprise subject to company-tax buys goods in Austria and sells them abroad ; (ii) when the same enterprise buys goods abroad through its foreign establishment and sells them in Austria. When the Austrian enterprise manufactures goods in Austria and sells them abroad, at least two-thirds of the total profits are subject to tax in Austria.

II. ALLOCATION OF PROFITS TO REAL CENTRE OF MANAGEMENT WITHIN THE COUNTRY.

The rules in this case differ from those governing the taxation of foreign enterprises operating in Austria. The law lays down that, as regards all Austrian enterprises whose activities extend to foreign countries, a minimum share of total profits shall be liable to Austrian tax. The quota varies according to the tax to which the enterprise is assessable. In the case of enterprises assessable to the general profits tax (see Part I, No. 2, page 15), at least one-quarter of the total net profit must be regarded as earned in Austria ; in the case of enterprises subject to company-tax, at least one-tenth of the total profits of the whole enterprise is liable to tax in Austria.

The minimum quota thus ascribed to the seat of management is calculated differently from the quotas previously mentioned. It is based upon the total income of the enterprise and not upon the partial receipts from certain specific transactions between the seat of management and the branch establishment.

This rule is based upon the view that the national enterprise, even when its operations are mainly foreign, nevertheless enjoys the same protection and advantages as an enterprise operating exclusively in Austria and liable to Austrian taxation only. It often happens that large export firms, which very likely have special need of this protection, pay quite insignificant taxes. For this reason, a minimum fraction of total profits is secured to the country of origin.

The fiscal conventions prescribe no minimum quota of this kind in favour of the central seat. The agreement with Hungary alone provides for one in the case of enterprises liable to company-tax.

Appendix to Sections A and B.

SPECIAL RULES LAID DOWN BY THE AGREEMENTS CONCLUDED WITH CZECHOSLOVAKIA AND HUNGARY REGARDING ALLOCATION OF PROFITS.

The methods of taxation described under A and B above have undergone certain treaty modifications. In all the treaties concluded by Austria, it is an accepted principle that the contracting States shall only tax enterprises within the limits of business done in the country itself. This means that, in principle, the contracting parties waive their right, under their own domestic law, to assess on a certain minimum fraction of total profits, whether in respect of the seat of the enterprise or of the separate establishments. (The fiscal treaty with Hungary, by way of exception, applies such minimum (*Sitzquote*) to the seat of enterprises liable to the company tax.) There is, however, nothing in the treaties which definitely settles how the profits assessable in the different countries according to the activities of the different establishments are to be determined. In this matter, therefore, there is unfortunately little improvement on the normal provisions of Austrian law. On this account, most of the Conventions provide for the conclusion of special allocation agreements which shall secure a uniform method of determining profits in both countries. The only agreements of this kind concluded so far are those between Austria on the one hand, and Czechoslovakia and Hungary on the other.

These agreements constitute for the countries concerned a new departure, although the arrangements in force between Austria and Hungary in the days of the old Austro-Hungarian monarchy (Agreement for the Avoidance of Double Taxation, *Imperial Law Gazette*, No. 278, 1907) constituted, to some extent, a precedent. According to those arrangements, the profits to be ascribed to the separate establishments of credit and insurance companies were determined by the fiscal authorities of the country in which the enterprise had its centre of management, and in accordance with the laws of that country. The figure as thus determined was then binding, for purposes of taxation, in the other country. This meant that the country in which the branch establishment was situated had indirectly to submit to the legislation of the other, and an administrative decision of the one State had immediate legal effect in the other State — a position incompatible with the full autonomy of two independent States and therefore not suitable for insertion without modification in the new post-war agreements. The agreements with Czechoslovakia and Hungary establish a system which avoids all encroachments by one national authority upon the administrative acts of the other, and, in principle, excludes overlapping between the two fiscal administrations. The fraction of total profits to be taken as the basis by each administration is fixed by agreement between the two Governments, but the determination of that total rests with the authorities of each State, though the two administrations give each other a large measure of mutual assistance. The system is perhaps of sufficient interest to merit more detailed description.

It was first introduced in relation with Czechoslovakia. As the result of the close economic relations between that country and Austria, dating back to their former existence as one State, many enterprises still maintain establishments in both countries, establishments having very close connections both on the technical and the commercial sides. And this has made it especially difficult to work out the accounts of the separate establishments in a manner to meet fiscal requirements. Allocation agreements were therefore felt as a particularly urgent need. They were concluded simultaneously with the fiscal treaty and were promulgated by Austria in the Decree of the Federal Minister for Finance, *Federal Law Gazette*, No. 3, 1923, and were completed at a later date by further arrangements concerning special allocation scales for credit and insurance institutions and the procedure adopted for the assessment of enterprises having establishments in both States (Decree of Federal Minister for Finance, *Federal Law Gazette*, No. 187, 1929).

The fiscal treaty with Hungary (*Federal Law Gazette*, No. 437, 1924) was similarly supplemented by special agreements (Decree of Federal Minister of Finance, *Federal Law Gazette*, No. 439, 1924), which were subsequently completed by administrative regulations (Decree of Federal Minister of Finance, *Federal Law Gazette*, No. 35, 1930). These special regulations were closely modelled on the arrangements made with Czechoslovakia.

Sphere of Application of the Allocation Provisions.

The arrangements apply to the taxation of profit-seeking enterprises maintaining establishments in Austria and in Czechoslovakia or, as the case may be, Hungary. The owners of these enterprises may be individuals or associations with or without legal entity. The establishments in the two countries, however, must belong to the same owner. This is, in practice, assumed to be the case when the same individual or company, or two partnerships without legal entity but composed of the same partners, own the enterprises in each country. If operations in the home country are in the hands of an independent national legal entity (*e.g.*, company by shares), even when the shares are held by a foreign company, identical ownership, as required for the execution of the agreements, is not as a rule assumed to exist.

Further, the application of these provisions is only practically effective when the establishments are establishments of the same business enterprise. This, however, is not the case, if the owner operates several concerns belonging to quite different branches of industry and working quite independently of one another.

Although the agreements do not expressly say so, the system is, in practice, confined to undertakings which keep regular books. It is sometimes doubtful whether the allocation provisions shall apply or not ; these cases must be settled on their merits by arrangement between the two countries.

Scales of Allocation.

In some of the most important forms of business activities (manufacturing, commercial, bank and insurance business), the profits to be ascribed for fiscal purposes to the separate establishments must be determined on the basis of schedular scales of allocation and without reference to the separate balance-sheets of the establishments. The basis for this determination is the total allocable profit of the enterprise. According to the interpretation of the agreements accepted by the Administrative Court, total profit means in each of the two countries total profit as determined by application of its own fiscal regulations (Official Collection of Judgments of the Administrative Tribunal : No. 13285, 1924 ; No. 13365, 1925 ; No. 14618, 1928).

Rules for Industry and Commerce. — The following rules of allocation were laid down, taking as a basis the minimum quotas used in Austrian and Czechoslovak fiscal practice :

In the case of the sales office of a manufacturing establishment situated in the other country, the commercial profit assessable against the office is one-third of the total profits from its sales.

If the sales office also makes purchases, its share is increased to one-half.

If purchases are made by the establishment in one country and sales effected by the office in the other country, the total profit from these operations is divided equally between the two.

The profit derived from the joint activities of the two establishments and allocable according to the above rules is determined from the total results of the enterprise on the basis of the ratio of the joint turnover of the two establishments to the total turnover of the enterprise.

If profits are earned exclusively by the activities of a single establishment, the amount thereof is ascertained from the total results on the basis of the ratio of the turnover of such activities to

the total turnover of the enterprise. Such profit is then subject to no further allocation. The different currencies are converted at average rates of exchange fixed according to special rules.

The above method of allocation may be illustrated by the following *example* :

The owner of an enterprise has a factory and a commercial establishment in Prague and a commercial establishment in Vienna. The articles manufactured at Prague are sold partly by the establishment at Prague, partly by the Vienna establishment. On the other hand, foreign products are bought by the Prague establishment and again are sold partly by that office, partly by the Vienna office.

Total turnover of the enterprise (S)	1,800,000 Schillings
Made up as follows :	
Sales of enterprise's own manufactures by office in Prague (S ₁)	500,000 Schillings
Sales of enterprise's own manufactures by office in Vienna (S ₂)	800,000 Schillings
Sales of foreign products by office in Prague (S ₃)	300,000 Schillings
Sales of foreign products by office in Vienna (S ₄)	200,000 Schillings
<i>Total profit</i> (T) determined according to the fiscal regulations	270,000 Schillings

Calculation from Point of View of the Austrian Fiscal Administration.

Total profit:

$$1. \text{ From manufacture : } \frac{S}{S_2} = \frac{T}{x}$$

$$x = \frac{S_2 T}{S} = \frac{800,000 \times 270,000}{1,800,000} = 120,000 \text{ Schillings}$$

of which $\frac{1}{3}$ goes to Vienna = 40,000 Schillings
 $\frac{2}{3}$ go to Prague = 80,000 Schillings

$$2. \text{ From purely commercial business : } \frac{S}{S_4} = \frac{T}{x}$$

$$x = \frac{S_4 T}{S} = \frac{200,000 \times 270,000}{1,800,000} = 30,000 \text{ Schillings}$$

of which $\frac{1}{2}$ goes to Vienna = 15,000 Schillings
 $\frac{1}{2}$ goes to Prague = 15,000 Schillings

Exclusively Czechoslovak profit:

= total profit less joint profit, that is :

$$270,000 \text{ Schillings} - (120,000 \text{ Schillings} + 30,000 \text{ Schillings}) = 120,000 \text{ Schillings}$$

... total Prague profit = 120,000 Schillings

Allocation of total profit between Vienna and Prague:

Vienna profit = 40,000 Schillings + 15,000 Schillings	= 55,000 Schillings
Prague profit = 80,000 Schillings + 15,000 Schillings + 120,000 Schillings =	215,000 Schillings
Total profit :	270,000 Schillings

Rules for Banks and for Insurance Companies. — In the case of branches of banks, that proportion of the total profits of the enterprise is allocated to the branch which corresponds to the ratio between the personnel charges of the branch and the personnel charges of the whole enterprise.

In the case of branches of insurance companies, allocation is made according to the ratio between the annual net premiums (less returned premiums or bonuses) paid to the branch and the total net premiums of the enterprise.

Rules for Other Kinds of Enterprises. — If a branch (in other than the above-mentioned cases) acts on behalf of a branch situated in the other country — such acts contributing towards the total results of the enterprise (e.g., an information office) — the profit from those activities is deemed by the State where they are exercised to be the customary business commission.

This rule, however, does not meet every case, so that the agreement, despite its detailed character, is incomplete. Its completion depends upon future developments.

Exceptions. — Profits are, in principle, allocated according to the scales agreed upon. The agreements, however, provide for the following exceptions :

The fiscal authorities of each country may agree to allocate according to the closed accounts, if allocation on this basis gives substantially the same results as are to be expected from allocation according to the above scales.

If the scales of allocation are obviously at variance with the actual results of operations, the fiscal administrations may, in a particular case, agree upon another principle of allocation after first hearing the views of the taxpayer.

Procedure for applying the Rules of Allocation.

Under the agreements concluded with Czechoslovakia and Hungary, the fiscal authorities have to follow a special procedure in the assessment of profits allocated as above.

In order that the principles and scales of allocation may be as uniform as possible, it is laid down that the fiscal authorities responsible for assessment in each country must communicate to each other the necessary fiscal data and furnish each other with any necessary legal assistance.

The procedure of assessment is as follows : the authorities in the country which proceed first to the assessment send the fiscal data to the authorities of the other State, which does not begin assessing until it has received these data.

In the case of enterprises subject to the company tax, assessment begins with the authorities of the State in which the enterprise has its seat of management ; in the case of enterprises liable to the general tax on profits, with the authorities of the State in whose territory the central accountancy is kept, or, if there is none, with the authorities of the State in which the owner of the enterprise resides. If this rule fails — if, for instance, the members of a partnership (*offene Handelsgesellschaft*) keeping no accounts reside in different countries — the question which authority shall assess first is a matter for agreement between the two Ministers of Finance.

Definite time-limits are fixed to prevent undesirable delays in these assessments. The authorities assessing first have to communicate direct to the assessment authorities of the other State, within six months of the expiry of the time-limit, the figures they have elicited as representing total profit and the separate profit of the individual establishments, the figures upon which tax is levied, the total turnover of the enterprise and the separate turnovers of establishments. In practice, this is generally effected by communication of the whole assessment material. The same data have to be communicated if there are any subsequent changes in the basis of the tax.

The assessment authorities of the other State have to issue the assessment notice for the fiscal period to which the communicated data refer within three months of the receipt of that communication. Any corrections of data communicated must likewise be notified to the authorities of the other State.

If these communications are not sufficient, special investigations can be set on foot in the form of legal assistance in the forms generally agreed upon (Treaty on Legal Protection and Assistance in Fiscal Matters, *Federal Law Gazette*, No. 81, 1929).

If requested, the authorities assessing first must extend the time-limit for appealing against a decision given on the basis of its allocation to thirty days from the issue of the demand note in the other State. This prevents an allocation accepted in one State from acquiring legal force before a decision has been given in the other State.

Should the assessment authorities fail to observe the time-limits fixed for assessment, the authorities of the other State need wait no longer before setting in motion their own assessment.

Practical Operation of System.

The agreements, which have been in force since 1923 in relations with Czechoslovakia, and since 1925 in relations with Hungary, have worked smoothly. The system has only taken real root since the introduction in 1929 of arrangements for legal assistance between the assessment authorities. It is only since data have been reciprocally exchanged that the assessment authorities have been able to obtain the material necessary for determining total profits and to fix the allocation scales in the two States on uniform lines.

Allocation according to the particular system usually takes place without regard to whether there are any special accounts or not. This obviates difficulties of checking, and the necessity, which often arises, of correcting the prices at which goods are invoiced as between separate establishments.

This method of allocation, as is inevitable under any method of averages, deliberately sacrifices individual accuracy. It is based on the fiction that similar activities in different establishments earn equal profits, although, as a matter of fact, commercial business in one State may be much more lucrative than in the other.

Nor are the scales of allocation graduated according to the different kinds of enterprise; they assume, therefore, that in all branches of industry the separate stages (manufacture and commerce) occupy the same relation to final results, though this is by no means necessarily the case. For instance, this relation may be different in the metal industries from what it is in textile manufacturing, and different for trade in home-produced semi-finished manufactures from what it is in the trade in home-produced finished goods.

As already mentioned, the total allocable profit is determined by each State according to its fiscal regulations. Even though the authorities in the two countries may fix the total profits at a different figure, the fact that, under the treaty arrangements, the several percentages add up to a hundred makes it impossible for the enterprise to be taxed in the different countries on more than its total profits. Where the fiscal regulations of the contracting States materially differ, real difficulties arise. Of these, the following are worthy of mention in relation to Czechoslovakia:

(a) Whereas, in the case of profit-making companies with separate legal entity, the company-tax is in Austria added to net profits as shown by the balance-sheet, in Czechoslovakia the special profits tax levied upon these enterprises is a deductible item. Hence the basis of allocation, even though the same material is used, is different in the two States, and the allocation quota adopted by the Austrian assessment authorities for purposes of Austrian tax is numerically larger than the quota arrived at in Czechoslovakia. This does not, however, constitute double taxation, but only means that the basis of taxation is determined more strictly under the laws of the one country than under those of the other. This, however, only affects the taxable quota of the country where the rules are stricter. Just as in the case of a wholly Austrian enterprise the whole of its profits are assessed on this stricter scale, so in the case of an enterprise half Austrian only half the profits are — quite rightly — so assessed.

Incidentally, the difference here referred to does not mean that the Austrian tax is higher, for the deduction of tax from profits allowed in Czechoslovakia is counter-balanced by a higher tax rate, while in Austria the addition of the tax to net profits is compensated by a lower rate.

(b) The ascertainment of total profits requires that, before allocation, all elements contributing to the business profits (items in the balance-sheet) must be estimated for fiscal purposes. The result of this is that even items which may be posted to accounts as a special fiscal privilege applying exclusively to operations within the country (*e.g.*, extraordinary depreciation of investments) can only be given consideration, in the State which grants this privilege, up to the amount corresponding to the allocation quota. If these extraordinary items are not posted to accounts in the other country the taxpayer may suffer hardship, which special inter-State agreements endeavour to mitigate.

C. HOLDING COMPANIES.

I. AUSTRIAN HOLDING COMPANY CONTROLLING ONE OR MORE FOREIGN SUBSIDIARY COMPANIES.

Austrian holding companies possessing in their portfolio shares of other companies, whether foreign or Austrian, are liable to taxation on their total income, which includes the distributions of their various subsidiary companies. However, only a fifth of the earnings distributed by subsidiary companies need be included in the taxable total, providing that at least one-fifth of one subsidiary company's shares is owned by the others. Further, there are certain provisions as regards the duration of the holding, and it is required that the subsidiary companies shall be engaged in the same branch of industry or commerce.

II. LOCAL SUBSIDIARY COMPANY CONTROLLED BY A FOREIGN HOLDING COMPANY.

The extent to which such subsidiary companies can be regarded as establishments of the foreign parent was explained in Part III, A and B.

Annex.

TARIFF OF TAXES.

I. INCOME TAX. ¹A. *Income not exceeding 14,400 Schillings.*

Amount of income in schillings		Percentage applicable to the total income
Exceeding	Not exceeding	
1,400	3,400	1.1
3,401	5,300	2.2
5,301	7,200	3.3
7,201	10,200	4.0
10,201	14,400	4.4

B. *Income exceeding 14,400 Schillings.*

Slice of income in schillings	Percentage applicable to each slice of income
From 1 to 14,400 schillings	4.4
For the following slice of 4,800.	6
For the following slice of 4,800.	8
For the following slice of 6,000.	11
For the following slice of 6,000.	14
For the following slice of 12,000.	18
For the following slice of 12,000.	22
For the following slice of 60,000.	27
For the following slice of 60,000.	32
For the following slice of 60,000.	38
For all further amounts	45

II. GENERAL PROFITS TAX. ²A. *Taxpayers of the First Group.*

Amount of income in schillings	Percentage applicable to the total taxable income
Not exceeding 4,800	1
Not exceeding 6,000	2
Not exceeding 7,200	3
In excess of this sum	4

¹ Paragraph 172 of the Law on Personal Taxes, *Federal Legal Bulletin*, No. 307, 1924, together with amendments.

² Paragraph 10 of the Law on Personal Taxes.

B. *Taxpayers of the Second Group.*

Amount of income in schillings	Percentage rate of tax applicable to the total taxable income
Not exceeding 10,800	5
Not exceeding 14,400	6
Not exceeding 18,000	7
In excess of that sum	7.5

C. *Minimum Rate.*

If the net income does not exceed the income tax minimum limit, the general profits tax is fixed at 10 schillings. In the case of registered firms (*Protokollierte Firmen*), the tax is at least 1.8 per mille of the net assets and in no case less than 420 schillings.

III. TAX ON SALARIES. ¹

Amount of taxable income in schillings		Percentage applicable to the total amount of the taxable sum
Exceeding	Not exceeding	
3,000	4,800	1.1
4,800	9,000	1.65
9,000	14,400	2.2
14,400	19,200	2.5
19,200	24,000	3
24,000	30,000	4
30,000	45,000	5
45,000	60,000	6
60,000	80,000	7.5
80,000		10

IV. COMPANY TAX. ²A. *Companies not subject to a Special Regime.*

Normal rate: Twenty-five per cent of the taxable income.

Minimum rate:

For companies other than insurance companies by shares; 3.6 per mille of paid up capital.

For insurance companies by shares; 3.6 per mille of the total net annual premiums, less premiums refunded bonuses.

In those two cases, the minimum tax may not be less than 420 schillings.

For mutual insurance companies; 3.6 per mille of the total net annual premiums, without any fixed minimum amount.

¹ Paragraph 41 of the Law on Personal Taxes.

² Paragraph 100 of the Law on Personal Taxes.

AUSTRIA (ANNEX)

B. *Savings Banks.*

Taxable income in schillings	Percentage rate applicable to the total income
Not exceeding 10,000	10
Between 10,000 and 30,000	17.5
Over 30,000	25

C. *Agricultural, Producers' Co-operatives, Building Associations.*

Amount of tax on income in schillings	Percentage rate of tax applicable to the total income
1 to 1,500.	Nil
1,500 to 3,000.	8
3,001 to 4,500.	10
4,501 and over	12

D. *Consumers' Co-operatives selling retail Foodstuffs and Household Commodities.*

Twelve per cent of the taxable income irrespective of the size of such income; an amount equal to one per cent of the turnover is, however, deducted from the taxable basis.

E. *Foreign Companies which are only taxed on their Income from Real Estate in Austria or participation in Austrian Profit-seeking Enterprises.*

Fifteen per cent of the net income.

V. TAX ON CAPITAL YIELD.¹A. *When collected at the Source.*

	Percentage
1. On the taxable income with the exception of the income mentioned under 2 to 4	10
2. Farm rents, land charges, yield of the lease of hunting-rights	15
3. Interest on bonds and certificates issued by the <i>Länder</i> , circles, communes, between January 1st, 1898, and December 31st, 1923; interest on bonds issued by the German Central Savings Bank; interest on mortgage bonds and bonds issued by the Austrian credit institute for enterprises of public works or public utilities; and on interest on deposits with savings banks and mortgage banks	5
4. Interest on savings deposited with co-operatives exempt from company tax or enjoying privileged treatment in respect thereof; interest on mortgages and loans guaranteed by mortgage banks; interests on scrips issued by savings banks	3

B. *When collected by Direct Payment:*

1. Farms rents, land charges and yield of the lease of hunting rights.	15
2. Other income	10

¹ Paragraph 131 of the Law on Personal Taxes.

BELGIUM

BY

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PART I. — GENERAL DESCRIPTION OF SCHEDULAR AND COMPLEMENTARY INCOME-TAX SYSTEM.¹

The system of schedular taxes on incomes was introduced in Belgium after the war² and has since constituted one of the chief sources of budget revenue. Out of an estimated total of more than 3 billions of francs for direct taxes, in the ways-and-means budget for 1933, schedular taxes account for approximately 1.7 billions, or 57 per cent. They amount to 19 per cent of the total fiscal revenue of the country in the same year (direct taxes, Customs and excise, registration).

The laws concerning schedular taxes on income establish the territorial character of the tax in respect both of incomes and persons. All income produced or received in Belgium is subject to schedular taxation, regardless of the domicile or nationality of the beneficiaries; on the other hand, persons domiciled or resident in Belgium are also taxed on income produced or received abroad. This twofold characteristic is expressed as follows in Article 2 of the co-ordinated laws²:

“ Tax is levied upon :

“ (1) The income from all real or personal property produced or received in Belgium, even if the beneficiary is not domiciled or resident in the country ;

“ (2) The income of persons domiciled or resident in Belgium, even if such income is produced or received abroad ”.

Domicile, Residence.

The notions of domicile and residence apply to individuals as well as to companies and partnerships.

An *individual* is domiciled in the place where his personal rights and interests have their centre — this is, as a rule, the place where his name is registered on the census or poll lists. It is also the place where he declares himself domiciled when executing a deed before a notary.

Residence, on the other hand, is the place where a person has the habit to live actually; it is a material situation which results from a stay of some duration. In most cases, domicile and residence are identical.

Companies and partnerships are domiciled in the place of their head office or principal establishment.³ The principal establishment is the establishment where the legal entity is centred, where the business is directed and controlled, the profits collected and meetings of shareholders held. In most cases this is also the head office and, when the statutes fix another head office, the latter is sometimes more apparent than real. In this case, the principal establishment is the place containing the chief factors of management or administration — *i.e.*, the offices, especially the managing offices proper, the commercial services and the central accountancy.

¹ Legislation in force on April 1st, 1933.

² Laws of October 29th, 1919, and August 3rd, 1920. These laws have since undergone considerable amendment. The result of the most recent co-ordination was published in the Belgian *Moniteur* on August 23rd, 1931.

³ Article 172 of the co-ordinated laws on commercial companies. Every company whose principal establishment is in Belgium is subject to Belgian law, even if the company was incorporated abroad.

Companies, Partnerships.

Under Belgian law, the term "share company" (*sociétés par actions*) applies not only to companies by shares (*sociétés anonymes*) and limited partnerships with share capital (*sociétés en commandite par actions*) established within the precise meaning of the co-ordinated laws on commercial companies, but also to similar companies, such as private companies (*sociétés à responsabilité limitée*), without distinction of nationality, provided, however, in all cases that they have their head office or principal establishment in Belgium and their capital divided into shares.

Accordingly, a share company, even if incorporated abroad, is subject to the regime governing similar Belgian companies, if it has its head office or principal establishment in Belgium.

Associations, other than share companies, which have legal entity, especially partnerships (*sociétés en nom collectif* and *sociétés en commandite simple*) are also taxable in Belgium if they have their head office or principal administrative establishment there; these associations are taxed as such on profits placed to reserve, but each partner is taxed separately on the sums allotted or distributed to him.

Foreign share companies and other foreign companies which have a branch, agency or any other establishment in Belgium are taxable in that country in respect of the profits resulting from any operations conducted by or through the said establishments.

There are three schedular taxes ¹ :

- (a) The tax on income from land and buildings ;
- (b) The tax on income from movable capital ;
- (c) The tax on professional income, this term being understood in its widest sense (industrial, commercial and agricultural profits, miscellaneous emoluments, profits from the liberal professions, legal functions and offices, and any lucrative employments).

I. TAX ON INCOME FROM LAND AND BUILDINGS.

(Articles 4 to 13, 33, 50 (paragraph 1), 51, 59 (paragraph 1, clause 2), 61, 65, 66 to 69, 72, 73, 74 (clause 2) of co-ordinated laws ; Articles 1 and 2 of the Law of July 23rd, 1932.)

1 and 2. TAXPAYERS AND TAXABLE INCOME.

This tax, representing in 1933 about 28 per cent of the yield from schedular taxes, is imposed upon income from any land or buildings situated in Belgium ; it therefore does not apply to property owned abroad by persons domiciled or resident in Belgium. ²

EXEMPTIONS.

Property is exempt from this tax if it fulfils the three following conditions : if it is national domain land ; if it is at the same time essentially unproductive ; if it is allocated to some public or public utility service.

Exemption is further granted to premises or parts of premises which an owner without any pursuit of gain may have devoted to the exercise of public worship, to education, or to the establishment of hospitals, hostels, clinics, dispensaries or similar charitable institutions.

¹ Until 1930, this system was supplemented by a tax on total actual income, called the super-tax; this was a personal tax and was not levied upon companies and partnerships. The Law of July 13th, 1930, abolished the super-tax and substituted for it the complementary personal tax, based either exclusively on expenditure indices or on a combination of indices and certain known forms of income, or exclusively on known income (see page 64).

² The income from such property is liable to personal property tax.

This tax is not collected for the first ten years after a house is built, provided the owner can furnish proof that building began after December 31st, 1927, and that the house was occupied before January 1st, 1931.

This remission is subject to certain conditions regarding sanitation and habitableness ; moreover, the cadastral income from these houses may not exceed certain maxima fixed according to the class of commune.¹

3. ASSESSMENT OF TAX.

(a) COMPUTATION OF TAXABLE INCOME AND ABATEMENTS.

The taxable or cadastral income (*revenu cadastral*) from land and buildings is determined by the competent authorities on the basis of an expert survey. It represents the ordinary average net income for one year — *i.e.*, the gross income less the following deductions for upkeep, repairs, etc. — one-fifth in the case of buildings ; one-tenth in the case of land.

The cadastral income is established by comparison with property of the same nature and similar yield situated in the same commune or in certain neighbouring communes selected as typical. The expert survey is made with due regard for the rent or for sale price and average rental value. If the taxpayer does not agree on the income ascribed to his property, the Administration and taxpayer may submit to arbitration of a third party, from whose decision there shall be no appeal, except on grounds of some material error.

Cadastral incomes are determined for a period of ten years.²

In each commune or cadastral section of commune, a yearly revision may, however, be made of the cadastral income of standard types of properties (*immeubles-types*) of each of the two categories (buildings and lands) or of one of the two categories only. If, for a category, the average of the revised income is greater or less, by at least 10 per cent, than the average of the income assessed for the current year, the cadastral income of all the parcels of the category may, by virtue of a Royal Decree, be reduced or increased by the same proportion as from the following year.

Revision is effected when an explanatory request is made before July 1st by the mayor or by a group of proprietors owning at least 10 per cent of the total number of the parcels of a category registered in the *Cadastral Record*. Revision may also be made by order of the Minister of Finance.³

(b) COMPUTATION OF TAX AND DEDUCTIONS.

The tax rate is fixed at 7 per cent.⁴ The provinces and communes may levy " *additional centimes* " on the tax thus computed.

¹ The exemption of ten years does not apply to (1) houses belonging to building companies approved by the National Housing and Cheap Houses Association or by the General Savings and Pensions Bank ; (2) houses sold by these companies to individuals at a discount ; (3) houses built by persons in receipt of a Government subsidy ; (4) houses built with war compensation or fire-insurance payments and country houses, holiday residences or premises for the sale of alcoholic beverages.

² The cadastral authorities are at present engaged in revising the survey of lands and buildings and it was originally intended that the income resulting therefrom should only be applicable for a period of five years. Article 1 of the Law of July 23rd, 1932, has, however, deferred the beginning of the new decennial period until January 1st, 1941.

³ Article 1 of the Law of July 23rd, 1932 (*Moniteur* of July 31st, 1932).

⁴ As a transitional measure during the years 1932 and 1933, the tax will be collected at the rate of 8 per cent on the cadastral income of lands in accordance with the existing situation on January 1st, 1930 (Article 2 of the Law of July 23rd, 1932) ; with regard to workshops, factories and, in general, buildings used for industrial purposes, the rate is raised during the same years to 9 per cent of the cadastral income which was used as a basis for the real property tax in 1931.

*Reductions.*¹

Reductions of tax are allowed, on request, to heads of families numbering at least three children; this reduction amounts to 7 per cent for each child dependent upon the taxpayer on January 1st of the fiscal year, but it may not exceed 200 francs per child.

Further, seriously disabled ex-servicemen may obtain a reduction of one-fifth of the tax levied on the house or part of the house they are occupying.

Finally, a reduction of one-quarter is allowed, on request and under certain specified conditions, in respect of houses occupied solely by the owner.²

An exemption or reduction of this tax may also be granted in proportion to the difference between the cadastral income of buildings and the actual income derived from them during the fiscal year, provided this difference amounts to at least 10 per cent of the real annual income.

4. COLLECTION OF TAX.

The tax is paid direct by the taxpayers concerned within two months³ of receiving the assessment notice. On request of the assessee, the tax may be charged to the tenants of the taxable property, on payment of a two francs fee for each extra notice sent out. In default of payment within the prescribed time-limit, the Treasury is entitled to interest on the sum due at 6 per cent per annum.

II. TAX ON INCOME FROM MOVABLE CAPITAL.

(Articles 14 to 24, 34, 50 (paragraphs 2 and 3), 51 to 59, 61 (paragraphs 3 and 5), 62 to 80 of co-ordinated laws.)

The tax on income from movable capital makes up the second schedule. In 1933, it yielded almost 37 per cent of the yield from schedular taxation.

1. TAXPAYERS.

This tax is an impersonal tax payable irrespective of the status, nationality and social or family circumstances of the individual, partnership or company that *pays* or *receives* income in Belgium. It is imposed upon all income from personal property — except such as is expressly exempted by special provisions enacted in the public interest — whenever that income actually materialises. Nevertheless, although the tax is applied without discrimination to all personal income and even to income from real property received abroad, its rate differs substantially according to the kind and origin of the income.

2. TAXABLE INCOME.

This tax is levied upon dividends, interest, annuities, and upon all other products of invested capital of whatever kind. These are divided into four main categories.

The tax is *in the first place* on income from shares of all kinds (*actions* or *parts*), bonds or other

¹ Claims must be submitted to the Directors of Taxes before October 31st of the year following the fiscal year, otherwise they lapse; but the period must not be less than six months from the date of the assessment notice or demand note.

² The cadastral income from these houses may not exceed 1,500 francs in communes with less than 5,000 inhabitants; 2,000 francs in communes between 5,000 and 30,000 inhabitants; 3,000 francs in communes with 30,000 and more inhabitants; these houses must be the occupants' only house property and they may not be used for the sale of alcohol.

³ This time-limit is reduced to one month in connection with taxes relating to 1932 and previous years (Law of December 30th, 1932, Article 2).

loans payable by commercial or non-commercial share companies having their head office or principal administrative establishment in Belgium.

Income from shares of all kinds includes dividends, interest, partners' shares, founder shares and all other profits distributed in any form and for any consideration whatsoever, also total or partial repayments of a company's capital as the result of profits.

If the company is wound up in consequence of liquidation or for some other reason, the tax is based on the total amount distributed in cash, bonds or otherwise, after deducting fully paid-up capital remaining to be refunded.

This capital is, if necessary, multiplied by a co-efficient fixed by Royal Decree, ¹ account being taken of the average rate of exchange in the year of payment.

When a company is dissolved without any distribution, the tax is payable on the real value of the company's property, subject to deduction as above.

This tax, however, will not be collected from share companies which are liquidated by way of merger before July 1st, 1935. ²

The *second category* of income assessable to personal property tax includes income from bonds issued by the State, provinces and communes and other public institutions or bodies, except as exempted by special legal provisions. ³

The *third category* of income liable to personal property tax is made up as follows :

(1) Capital invested in any commercial, industrial or agricultural, concern, operated otherwise than by the companies in the first category, and excluding capital invested either by an owner in his own business or by managing partners in partnerships having legal entity.

The collection of personal property tax is therefore limited to the income from capital invested in any commercial, industrial or agricultural enterprise by *non-active* partners, especially sleeping partners, who only contribute funds, securities or property, even though they may intervene from time to time as legal or technical advisers, etc., to the association.

(2) All loans and debts to the charge of individuals and companies other than share companies, resident or domiciled in Belgium.

The income from debts and loans includes income :

(a) From any debts owing by Belgian companies other than share companies ;

(b) Of individuals, groups, or *de facto* associations engaged in industry, trade or any kind of enterprise in Belgium ;

(c) Of foreign share companies having an establishment in the country.

(3) Sums of money deposited in Belgium with banks, exchange, credit, deposit or savings institutions, or with bankers, notaries, business agents or other depositaries.

The tax is payable on the income from these deposits whoever the depositaries may be, and irrespective of the domicile or residence of the depositor and of the duration and nature of the deposit (guarantee, surety, or consignment).

Nevertheless, debts or deposits of a professional character are exempt, if it is duly shown that the interest thereon is included in the accounts of the beneficiary enterprises situated in Belgium (Article 18, last clause of co-ordinated laws).

The *fourth category* includes income from foreign debentures and securities, foreign debts, cashed or received in Belgium by any person whatever or cashed or received abroad by individuals or legal entities domiciled or resident in Belgium.

¹ Royal Decree of September 5th, 1930 (*Moniteur* of September 14th, 1930).

² Article 4 of the Law of July 23rd, 1932 (*Moniteur* of August 7th, 1932).

³ These provisions were voted in order to encourage investment in certain national loans.

Under certain conditions fixed by the Minister of Finance, the tax is not payable on income from foreign securities deposited in Belgium by individuals or legal entities having in Belgium no domicile, residence or establishment.

The tax also applies to the yield from the lease, use and concession of any personal property and to income from real property situated abroad.

Income from Colonial Enterprises.

The Law of June 21st, 1927, created a special regime in favour of enterprises operating in the Belgian Congo.

In principle, enterprises — whether they have or not the form of companies — which have their head office or principal administrative establishment in Belgium and their centres of operation in the colony, are liable to taxes on income, regardless of whether the taxable income is of Belgian or colonial origin.

The tax is imposed: (a) in the case of share companies, on the income from share and on profits placed to reserve or on one-twentieth of the annual net profit in the case of Congo private companies (*sociétés à responsabilité limitée*); (b) in the case of other taxable enterprises, on income distributed to members or partners or on other income from invested capital.

The rate of the tax is 17 per cent for the incomes enumerated above; it is reduced to 13 per cent on income from bonds.

The Colonial Treasury receives the whole of the tax on the interest on colonial loans and on dividends accruing to the Government of the Belgian Congo from securities in its portfolio, and four-fifths of the capital yield of the other taxes on securities, including the tax on income from bonds; the remaining fifth goes to the Belgian State.

3. ASSESSMENT OF TAX.

This tax, being an impersonal tax, is levied on all income without regard to the person who pays or receives it (see page 52); consequently no deduction is allowed, either from the taxable basis or from the amount of tax, by reason of family charges or other considerations based on the status, nationality or social circumstances of the person who pays or receives such income.

If income is fixed in a foreign currency or is payable abroad, the amount is converted into francs at the rate of exchange at the time of payment, prior to assessment (Article 19).

Further, any tax paid by the debtor in discharge of the beneficiary of the income is added to the latter, for purposes of tax assessment (Article 14, paragraph 2).

The rate of the tax varies between 2 and 22 per cent, according to the table of tariffs (see Annex).¹

4. COLLECTION OF TAX.

As a rule, tax is collected by deduction at the source at the time when the income is paid. It is paid into the Treasury within a fortnight of the attribution or payment of the income; in default of payment within this time-limit, the Treasury is entitled to charge interest on the sum due at the rate of 6 per cent per annum.

The provinces and communes may only levy additional tax (*centimes additionnels*) on income from capital invested in Belgium.

¹ Article 7 of the Law of March 23rd, 1932 (*Moniteur* of March 26th), establishes for 1932 and 1933 an additional tax of 10 per cent of the tax on income from personal property. However, as regards income of foreign origin, received abroad, this additional tax will only be levied on the tax payable on income ascribed or made payable after April 1st, 1932.

III. TAX ON PROFESSIONAL INCOME.

(Articles 25 to 32, 35, 50 (paragraphs 4 and 5), 51 to 59, 61 (paragraphs 3 and 5), 62 to 80 of co-ordinated laws ; Article 5 of the Law of July 23rd, 1932 ;¹ Articles 7 and 8 of the Royal Decree of January 13th, 1933.²)

The tax on professional income, or professional tax, forms the third schedule. Although, in 1933, its yield was equal to that of the tax on income from personal property (37 per cent of all schedular tax yield), it is of more importance for the purposes of the present study.

The professional tax is partly impersonal and partly personal, for, while it is imposed upon income whenever earned, deductions both from the taxable basis and the amount of tax depend upon the status of the beneficiary.

1. TAXPAYERS.

Professional tax is payable by all individuals or legal entities, associations without legal entity and *de facto* associations :

(a) Who derive income in Belgium from any industrial, commercial or agricultural enterprise (including profits from the personal work of members of commercial or non-commercial companies having a legal entity separate from that of the members), or profits of any kind whatever from the liberal professions, functions, offices or any lucrative employment ;

(b) Who make various payments in Belgium (salaries, wages, pensions, annuities, directors' percentages, fees to auditors or liquidators of share companies), even if the recipients of these payments reside abroad or in the Belgian Congo.

The professional tax on the different payments under (b) is collected at the source and therefore raises no difficulty. The treatment of the taxpayers referred to under (a), however, calls for certain explanations.

It was said at the beginning of this chapter that, in Belgium, the fiscal regime applying to the Belgian taxpayer domiciled or resident in Belgium is applied *ipso facto* to a foreigner engaged in business in Belgium, whether an individual or a company other than a share company. Foreign share companies operating in Belgium are expressly taxable at the fixed rate of 10 per cent (plus provincial and communal additions) on all profits earned by their Belgian establishments.

The regime applicable to Belgian share companies and foreign share companies differs therefore as follows. Belgian companies owe the tax on income from personal property on distributed income, and professional tax on a graduated scale (maximum of 9.9 per cent, plus provincial and communal additions) on other profits, while foreign companies are only liable to professional tax at the fixed rate of 10 per cent³ (plus provincial and communal additions) on all profits from Belgian sources.

Colonial Companies.

The Law of June 21st, 1927, as was seen (page 54), created a special system in favour of enterprises operating in the Belgian Congo. That law lumps together profits earned in Belgium and the Congo and subjects them to a combined tax, the yield from which is divided between the colony and the home country.

After the collection of the tax on income from personal property on income liable thereto, the professional tax is levied at the ordinary rates on remaining profits, except on reserves invested in the colony within the previous five years.

When colonial enterprises have operating centres abroad or work up Congo products in Belgium, the profits earned by these centres or establishments are subject to the ordinary rules of taxation.

¹ *Moniteur* of July 31st, 1932.

² *Moniteur* of January 15th, 1933.

³ See note 1, page 54.

One-fifth of the State's share in the taxes on profits of the said establishments earned in Belgium accrues to the Colonial Treasury.

National Enterprises operating abroad.

When a taxpayer has his head office or principal establishment in Belgium and establishments abroad, he is taxed on all profits realised both in Belgium and abroad.¹ Nevertheless, the results of the Belgian and foreign operations must be considered separately, although with due regard for the results of the general balance-sheet. For this purpose, the taxpayer concerned must attach to his annual declaration, not only the general accounts, but a copy of the separate balance-sheet and profit-and-loss account relating to the business of the separate foreign establishment (Article 54, paragraph 1, (3)). These last profits are taxed in Belgium at a reduced rate, if they have already been taxed abroad (Article 35, paragraph 7).

It does not matter whether or not the foreign establishments are *de facto* dependent upon the centre of management in Belgium.

In the case of an *individual*, the whole of the profit is liable to professional tax, subject to a reduction of rate for income earned and taxed abroad.

On the other hand, in the case of a *company or partnership*, professional tax on total profits is subject to the deduction of distributed income or of income liable to personal property tax as income from invested capital ; both taxes, moreover, are levied at reduced rates on profits earned and taxed abroad.

Foreign Enterprises deriving Income from Belgian Sources.

In principle, foreign enterprises are only taxable in Belgium if they have one or more *establishments* in the country, at whose head office they are bound to keep separate accounts of the business transacted by or through these establishments. The only deductions allowed under the head of general or administrative expenses are expenses of this kind incurred by the said Belgian establishments (Article 27, paragraph 4).²

The word *establishment* must be understood in its broadest sense : a place of business, an agency and a branch constitute establishments within the meaning of the law. The existence of a board of management and staff is not essential. This definition covers industrial and commercial establishments and insurance companies, which are, by common knowledge, publicly represented in Belgium by authorised agents.

A foreign enterprise operating in Belgium through an establishment is liable to professional tax at the rate, and according to the rules, applying to Belgian taxpayers of the same class. Only the profits of the Belgian establishment of a foreign share company pay the uniform rate of 10 per cent.³

A special regime applies to *representatives of foreign firms, foreign bargemen, itinerant vendors, etc.* Subject to any exceptions provided for in international conventions, the professional tax is fixed at a minimum of 200 francs in respect of representatives of foreign firms, foreign bargemen, itinerant vendors, hawkers and other persons who carry on their business in Belgium, without having any domicile, residence or establishment in the country. The tax is paid before engaging in the

¹ These taxpayers have to arrange with the Fiscal Administration for the acceptance of a real surety or personal guarantee (Royal Decree of February 18th, 1920 ; *Moniteur* of March 5th, 1920).

² Foreign companies and all other foreign taxpayers having in Belgium one or more establishments of any kind, such as operating centres, branches or agencies, have to obtain from the Fiscal Administration approval of at least one responsible representative established in the country and able to furnish the necessary guarantee of solvency. In the event of a breach of this provision, the Minister of Finance may order the Belgian establishments to close and forbid those concerned to engage in any business in Belgium until they have complied with the regulations.

³ See page 54, note 1.

business in Belgium. If, however, the resultant income justifies a higher tax, a proportionate supplement may be demanded (Article 27, paragraph 4).

Foreign Shipping Companies.

In principle, foreign shipping companies whose vessels land in Belgium are liable to income-tax. The Government, however, is empowered ¹ to conclude international conventions granting on a basis of reciprocity full exemption from income-tax to foreign shipping enterprises not domiciled in Belgium.

Conventions of the kind have been concluded with Norway, Denmark and Iceland, Finland, Ecuador, Sweden and France.

Negotiations are proceeding with other countries.

2. TAXABLE INCOME.

The following is deemed to be taxable income :

(a) *Profits of any Industrial, Commercial or Agricultural Enterprise, including Profits from the Individual Work of Members of Commercial or Non-commercial Companies having Legal Entity.* — The profits of industrial, commercial or agricultural enterprises are those resulting from any operations conducted by or through their establishments.

For purposes of professional tax, the law expressly considers as profits :

- (1) The remuneration received by the *entrepreneur* for his personal work ;
- (2) The profits and advantages which he derives in kind ;
- (3) The profits from his speculations ;
- (4) Sums devoted to the total or partial repayment of borrowed capital, the extension of the enterprise or the improvement of plant ;
- (5) Reserves and provision of any kind, annual carry-forward and similar appropriations.

Nevertheless, tax is only imposed upon the half of profits actually employed, within the country and within twelve months of the close of the trading year, on the building of workmen's houses or installations on behalf of the staff of the enterprise.

Taxable income further includes personal expenditure, such as the rent of premises used for living purposes, the upkeep of the taxpayer's household, cost of education and any other expenses not necessitated by the exercise of the profession or occupation.

The income enumerated above is taxable on its net amount — that is, on the gross amount less only such professional expenses as have been incurred, during the fiscal period, for the purpose of acquiring and maintaining that income.

The following, *inter alia*, are regarded as *professional charges* :

- (1) The rental value, actual or presumed, of premises or parts of premises set aside for the exercise of the profession and all general costs resulting from their upkeep, heating, lighting, etc.;
- (2) Interest on capital borrowed from third persons and invested in the enterprise, and any charges, annuities or similar payments in respect thereof ;
- (3) Salaries and wages of employees and workmen in the service of the enterprise ;
- (4) Necessary depreciation allowances for the material and chattels used in the business, provided that such allowances correspond to actual depreciation during the fiscal period.

Depreciation allowances are based upon investment value or cost price.

Nevertheless, as regards business premises and industrial, commercial or agricultural plant acquired or constituted before July 1st, 1926, depreciation allowances may be based upon a cost

¹ Article 2 of Law of July 14th, 1930 (*Moniteur* of September 6th, 1930).

price re-assessed under conditions and within limits to be fixed by Royal Decree; this re-assessment must be entered in the closed accounts or balance-sheets of 1931 at the latest.¹

(b) *Miscellaneous Remunerations.* — The co-ordinated laws of Belgium concerning income-taxes also subject the following *miscellaneous remunerations* to professional tax :

(a) All payments made by a third party to persons who are bound by no business contract, including pensions and annuities ;

(b) Payments to directors, auditors or liquidators of share companies, including governors, managers, *régents*, *censeurs*, and others discharging similar functions.

Advantages in kind are added to remunerations or wages ; they are computed at their actual value or are re-assessed at a flat-rate, according to circumstances.

From these remunerations it is permissible to deduct sums withheld as contributions to pensions or insurance funds, and professional expenses. In the absence of evidence — and generally there is none — these charges are fixed at one-quarter if the emoluments are less than 15,000 francs and at one-fifth if they exceed that amount (with a minimum of 3,500 francs). This fixed sum, which includes the taxes deductible as professional expense, may not exceed the amount of such taxes by more than 30,000 francs.

Taxable emoluments do not include :

(1) Family grants or allowances to children, up to an amount equal to the similar allowances permitted to State officials and employees ;

(2) Pensions, annuities and compensation granted under the old-age pension laws ; relief granted to premature disablement or death, pensions to disabled persons, widows, orphans and ascendant relatives of service men, victims of occupational accidents and congenital cripples ;

(3) Prizes, grants, annuities or pensions allowed to artists, *savants*, etc., by the public authorities or official bodies, excluding sums paid for services rendered.

(c) *Profits from the Liberal Professions, etc.* — Lastly, the Belgian fiscal regulations subject to professional tax *the profits of any kind whatever from the liberal professions, functions and offices and any lucrative employment.*

These profits consist of the difference between total receipts and expenses attaching to the exercise of the calling.

Failing proof to the contrary, these expenses are fixed at one-fifth of the said receipts, but this amount may not exceed by more than 30,000 francs the taxes deductible as professional expenses.

Persons engaged in the liberal professions or fulfilling functions or offices are required, under penalty of a fine of 500 francs for each infringement, to furnish a signed and dated receipt of their fees, commissions or other emoluments.

This receipt is taken from a book with counterfoils, the model for which is prescribed by the Minister of Finance. The latter may demand that entry be made in the counterfoils and leaves of this book only of the total amount of fees, commissions or emoluments and the name of the person from whom they were due.

Any person making a payment of this kind without demanding the receipt is liable to the fine jointly with the person concerned.

The issue of a receipt is not compulsory for professional persons if they keep a classified daily record of their professional receipts and expenses. Any omission to do this makes them liable to the fine mentioned above.

¹ This question is settled in the Royal Decree of October 12th, 1930 (*Moniteur* of November 5th, 1930).

3. ASSESSMENT OF TAX.

(a) COMPUTATION OF TAXABLE INCOME.

General Rules.

The Belgian fiscal system is based upon the principle of an annual declaration of income.

Generally speaking, all those liable to the three classes of professional tax have to submit, during the first three months of the year, the return required under Article 53 of the law to the Tax Controller within whose jurisdiction they have their principal establishment or are domiciled or resident.

But taxpayers whose accounts do not cover the calendar year, and also all share companies, have to forward to the Controller of Taxes, within a fortnight of the approval of the balance-sheet and profit-and-loss account and, at the latest, within six months of the close of the trading year, a return containing, according to categories, the total income liable to the tax on income from personal property and professional tax. This return must be accompanied by a copy of the balance-sheet and profit-and-loss account, of the resolutions approving them and the Minutes or reports relating thereto; further, by a list showing the number and amount of shares and bonds issued and of securities of one kind or another bought or sold during the past financial period, and by a copy of the separate balance-sheets and profit-and-loss accounts of any separate foreign or colonial establishments.

Failing documentary evidence furnished either by the taxpayer or by the Administration, taxable profits are determined for each taxpayer by comparison with the normal profits of persons similarly placed and with due regard, according to the circumstances, for capital invested, turnover, number of workmen, motor-power used, rental value of exploited land and any other useful information. The Administration may, for this purpose, agree upon empirical bases of taxation with the professional associations concerned.

No division of profits from joint operations is allowed between members of the same family living together or between the members of any company, association or community. However, the emoluments of members of the family of an *entrepreneur* working with him are included among general costs, provided they do not exceed a normal wage or salary and provided they have been assessed as such to professional tax (Article 27, paragraph 3).

The tax is payable by the head of the family or by the director of the company, association or community.

Professional tax, in the case of share companies, is levied upon their profits less income distributed or liable to personal property tax as income from invested capital (Article 35, paragraph 2).

In order that the same income may not be taxed twice, Article 52 of the co-ordinated laws provides for the deduction from schedular taxes of all direct or additional taxes which the taxpayer may already have paid in Belgium on taxed income, or which share companies with their head office or principal establishment in Belgium may have already paid there on sums distributed as shares.

As regards companies other than share companies, including partnerships, having a legal entity, each member is liable separately, in respect of sums allotted or distributed to him, to professional tax if he is an active partner, or to personal property tax in other cases.

The company or partnership is liable to professional tax in respect of profits placed to reserve, the provisions of Article 52 being applicable to this case also.

The professional tax is on income, actually determined or presumed, either for the previous year, in the case of taxpayers whose accounts coincide with the calendar year, or, in the case of other taxpayers, for the twelve months covered by the accounts of the current year.

The income for the year or taxable period, as the case may be, is subject to deduction of any professional losses incurred during the two preceding years or financial periods. Thus a taxpayer, whether an individual, a partnership or a company, who keeps regular accounts and suffers professional losses during the past two years or financial periods may deduct these losses from the profits of the year following.

National Enterprises operating abroad.

In determining profits earned abroad, the only deductions are the overhead expenses of the establishment and the taxes paid in the country where it is situated.

The general or administrative expenses of the head office in Belgium, even when incurred on behalf of a foreign establishment, must be placed to the account of Belgian operations. This applies to directors' and auditors' fees and to bond coupons; however, the amount of the coupons must be accounted to the foreign establishments if the bonds are issued abroad and for the requirements of the foreign establishments.

Profits derived from operations directed by the taxpayer from the head office in Belgium without the intervention of agents or establishments abroad are not regarded as having been earned abroad. Thus, profits from reinsurances contracted by a Belgian firm with a foreign insurance business are regarded as Belgian profits; so are the profits from speculations figuring in the head office's portfolio and consisting in the repurchase of bonds below par.

Foreign Enterprises deriving Income from Belgian Sources.

In principle, foreign enterprises which derive income from operations in Belgium are taxed on the results of their specifically Belgian operations as shown by the separate accounts they have to keep, even when the general balance-sheet reveals a loss. If the accounts fail to supply the necessary evidence,¹ the enterprise is taxed on a minimum profit fixed by the Royal Decree of October 8th, 1930.²

It is therefore necessary to separate from the results of the balance-sheet, the profits (dividends, increases of capital, reserves, writings-off of foreign losses, etc.) realised by the Belgian establishment, which constitute the taxable basis.

If specific capital is set aside for the establishment in Belgium and the latter has a special account and a separate balance-sheet in the enterprise's accounts, that special account and separate balance-sheet, duly checked, form the basis for determining the taxable profits.

Profits expressed in foreign currency are converted, if necessary, into Belgian money at the official rate of exchange at the date on which the accounts in question were closed.

Foreign Insurance Companies. — Foreign insurance companies operating in Belgium are not required to apportion their profits according to the class of policy (life insurance, temporary, mixed, etc.), but only according to the branch of insurance (life, fire, etc.).

These companies must include in their accounts:

(a) The gross premiums³ paid to their Belgian agencies, without deduction of premiums surrendered to reinsurance companies;

(b) The reserves corresponding to policies concluded by these agencies or contracted in Belgium by agents domiciled abroad, mention being made of any mathematical and special reserves existing at the beginning and end of the business year;

(c) Interest on the premiums and reserves referred to under (a) and (b), irrespective of whether they are invested in Belgium or abroad by the agencies or by the head office;

¹ These accounts may consist of the books mentioned in Article 16 of the Law of December 15th, 1872 (Commercial Code). In any case, they must furnish the material for drawing up and checking either the separate balance-sheet and profit-and-loss account of the establishments, or a summarised statement showing by classes the volume of the different operations of these establishments and the profits derived therefrom.

² Royal Decree of October 8th, 1930 (*Moniteur* of October 19th, 1930), (see page 79). This empirical system is not compulsory when the Administration is in possession of comparative data which enable it to fix the taxpayer's liability on a basis more in accordance with facts.

³ The term "gross premiums" includes all premiums due, whether paid or not, after deduction or cancelled premiums, but without previous deduction of commissions, brokerage, fees or other expenses.

(d) Compensation paid by the Belgian agencies ;

(e) Overhead expenses of these agencies including costs of inspection (fees, travelling expenses, subsistence allowances, etc.) in connection with losses falling upon them and included in their accounts.

The accounts of foreign insurance companies must also mention any reinsurance business relating to policies concluded by the Belgian agencies or contracted in Belgium by agents domiciled abroad, if those agencies intervene in any way in the surrender of premiums to reinsurance companies, the payment of that part of losses refunded by the latter, the collection of reinsurance commissions, etc.

In order to ensure the requisite uniformity in the taxation of foreign insurance companies, the Administration has ordered the use of a standard profit-and-loss account containing all the information required.

Foreign Firms selling Imported Goods in Belgium, or re-exporting them abroad. — The profits from these operations are determined in Belgian francs, after deducting from the price of sale or re-consignment :

- (a) The value of the goods at the moment they are consigned from abroad ;
- (b) The cost of transport as far as Belgium, including insurance and import duties ;
- (c) Any costs of handling, storage, housing or packing incurred in Belgium prior to sale or re-consignment ;
- (d) Other overhead expenses incurred in Belgium in connection with these operations.

(b) COMPUTATION OF TAX AND DEDUCTIONS.

Professional tax is levied on the total annual income of each taxpayer or, for periods of less or more than one year, on any proportionately equivalent sum.

It is not due when the taxable income is below the following minima :

- 4,800 francs in communes with fewer than 5,000 inhabitants ;
- 5,600 francs in communes with from 5,000 to 30,000 inhabitants ;
- 7,200 francs in communes with 30,000 or more inhabitants.

The commune taken into consideration is either that in which the calling is exercised or that in which the taxpayer is domiciled or resident, whichever he prefers.

The above minima are increased to take account of a taxpayer's dependents. ¹

In the case of taxpayers whose professional income does not amount to 50,000 francs, the tax varies from 12 francs to 2,256 francs, according to the size of the income and on a sliding scale fixed by Royal Decree according to the class of commune. ²

¹ The increase is one-fifth for each member of the family dependent on the taxpayer on January 1st of the fiscal year. If there are more than two children in the family, the increase, whatever the population of the commune, is fixed at 2,500 francs for each child in excess of two, at 4,000 francs for the fifth and sixth children, and at 5,000 francs for every child above six. The rate of increase in respect of the taxpayer's wife is equal to that in respect of the last child. If the taxpayer is a widower or widow, the dead spouse is deemed to be alive for purposes of calculating the exempted minimum.

² Royal Decree of July 18th, 1930 (*Moniteur* of July 30th, 1930). Nevertheless, Article 7 of Law of March 23rd, 1932 (*Moniteur* of March 26th, 1932), fixes for 1932 and 1933 a special tax of 10 per cent (exclusively in favour of the State) on the professional tax payable on taxable incomes of 35,000 francs and over.

In the case of taxpayers with a professional income of 50,000 francs or more, the tax is computed on the following scale¹:

Net income of :	Percentage of tax
50,000 and less than 60,000	5
60,000 and less than 70,000	5.5
70,000 and less than 90,000	6
90,000 and less than 110,000	6.5
110,000 and less than 130,000	7
130,000 and less than 150,000	7.5
150,000 and less than 175,000	8
175,000 and less than 200,000	8.5
200,000 and over	9

On the tax thus computed, reductions are granted in respect of family charges.²

In the case of industrial, commercial and agricultural profits exceeding 50,000 francs net, the professional tax is increased by one-tenth, with a minimum increase of 18 francs.

When these profits are between two-thirds of the exempted minimum and the minimum mentioned above, tax is collected at a flat rate between 10 and 25 francs on a scale fixed by Royal Decree.³

By way of exceptions to the above rates, the tax is uniformly fixed at :

- (a) Ten per cent for the profits of foreign share companies ;
- (b) Nine per cent for the fees of directors, auditors, liquidators, governors and others exercising similar functions, belonging to Belgian, foreign or colonial share companies; the part of the tax corresponding to these fees is increased by 100 additional centimes.⁴

Nevertheless, as regards directors, etc., who actually exercise, by election or appointment, real and permanent functions in the same company, the ordinary regime of the law remains applicable to all fixed or determinable remuneration paid to them by the said company, in so far as this remuneration exceeds the fees paid to their colleagues not vested with special functions. The part so subject to the ordinary regime of the law may not exceed for each taxpayer and company either 100 per cent of the net profit on which the statutory percentages have been computed or 100,000 francs if the application of the said percentages gives an amount less than 100,000 francs.

If all the directors, as well as those officers who can be assimilated to directors, exercise special functions in the same company, that part of the remuneration susceptible to the regime of ordinary law may not exceed for each taxpayer and company either 0.75 per cent of the above-mentioned net profit, or 75,000 francs if the application of the said percentages gives an amount less than 75,000 francs.

The remuneration is reckoned at its gross amount — *i.e.*, without deduction of the amount allowable as actual or estimated professional expenses.

The possible exception of the 100 "additional centimes" may not be granted in connection with more than two companies to be designated by the interested parties in their annual returns.

The withholding of the tax, and the "additional centimes" connected therewith, at the source is regulated by Royal Decree.⁵

¹ See note ² on page 61.

² The tax is reduced by 5 per cent for each member of the family dependent upon the taxpayer on January 1st of the fiscal year. This rate is increased to 7 per cent for each child after the third. The deduction thus calculated may not exceed 700 francs per dependent.

³ Royal Decree of July 18th, 1930 (*Moniteur* of July 30th, 1930).

⁴ The Treasury of the Belgian Congo is allowed annually a sum equal to 2 per cent of the total fees granted to directors, auditors, liquidators or others exercising similar functions on behalf of Belgian companies operating in the colony or incorporated under colonial law (Law of June 21st, 1927).

⁵ Royal Decree of July 20th, 1931 (*Moniteur* of July 26th, 1931).

The tax, computed according to the ordinary scales, is reduced to one-fourth for that part of the taxable income which is earned and taxed abroad.

The provinces and communes are allowed to levy "additional centimes" tax on the professional tax on industrial, commercial, agricultural and similar profits and on profits from the liberal professions, functions or offices realised *in Belgium*; these "additional centimes" may not be added to the tax on profits earned and taxed abroad or in the Belgian Congo.

The communes only may levy a special tax on wages, salaries and pensions.

No provincial or communal tax may be levied upon the fees of directors, auditors, liquidators, etc., of share companies already liable to the 100 "additional centimes" imposed in favour of the State.¹

4. COLLECTION OF TAX.

(a) BY DIRECT PAYMENT.

Professional tax on industrial, commercial and agricultural profits and on profits from the liberal professions, functions and offices is payable within two months² of receiving the assessment notice or demand note. The Treasury is entitled to charge interest on sums due at 6 per cent per annum.

Taxpayers may appeal against their assessments to the provincial or district Director of Taxes.³

The Controller assesses tax on the declared income unless he deems it an incorrect figure. In this case, he may correct it on informing the taxpayer, before assessment, of the figure he proposes to substitute for the figure declared and giving the reasons for the alteration. The taxpayer is given twenty days in which to submit observations. If the parties still disagree, the dispute may be submitted to a Committee which sits in the chief town of each control area, and whose composition and functions are determined by Royal Decree.³

The Committee's opinion, with reasons for it, is notified to the taxpayer by the Controller, who also informs him of the income figure upon which he proposes to assess tax.

If this figure coincides with the opinion of the Committee, the taxpayer can only obtain a reduction by furnishing proof of the exact amount of his taxable income.

In the contrary event, the burden of proof is upon the Administration, if the income taxed is in excess of the Committee's estimate.

The Committee must also be consulted before any *ex-officio* assessment is made.

(b) BY DEDUCTION AT THE SOURCE.

Professional tax on the various remunerations is collected by withholding the amount due at the time of payment; the law prescribes that the persons responsible for paying the income may deduct therefrom the tax due, subject to no appeal by the beneficiaries, whatever their nationality. This deduction is effected on a scale fixed by Royal Decree;⁴ the tax thus withheld must be paid to the receivers of taxes within a fortnight of the end of the month in which the income was paid. The control of payments and any adjustment of the fiscal position of the taxpayers concerned are effected by means of individual forms filled up by the employer. These forms are issued to the person in receipt of the salary, wage, etc., and attached by him to his annual declaration.

¹ See note 2 on page 61.

² See note 3 on page 52.

³ Royal Decree of October 12th, 1930 (*Moniteur* of November 5th, 1930).

⁴ Royal Decree of July 18th, 1930 (*Moniteur* of July 30th, 1930). See note 2 on page 61. As regards professional tax collected by deduction at source on income other than that of the directors, etc., of share companies (Article 25, paragraph 1, clause 2 (a) and (b)), the 10 per cent additional tax is only applicable to the tax on income allotted or paid since April 1st, 1932. Adjustment of a taxpayer's fiscal situation is effected without regard to the additional 10 per cent thus deducted at source.

In the case of persons who receive professional income of different kinds, tax is computed on the total income for the previous year after deduction of any taxes collected at the time the income was paid.

IV. COMPLEMENTARY PERSONAL TAX.

(Article 37 and following of co-ordinated laws ; Articles 6 and 7 of the Law of July 23rd, 1932 ; Articles 1 to 6 of Royal Decree of January 13th, 1933, in execution of Article 1 of the Law of December 30th, 1932.)

Until 1930, the income-tax system included, in addition to the schedular or impersonal taxes, a personal tax called complementary income-tax or super-tax, payable by the taxpayer in respect of his total income — *i.e.*, the total income directly or indirectly subject to schedular taxes and income exempt from these taxes.

The Law of July 13th, 1930,¹ modified by Articles 6 and 7 of the Law of July 23rd, 1932, and by Articles 1 to 6 of the Royal Decree of January 13th, 1933, issued in execution of the Law of December 30th, 1932, replaced the super-tax on total actual income by the complementary personal tax, based in principle on a number of expenditure indices common to the majority of taxpayers and indicating the apparent station in life — rental value of house and furniture, number of servants, horses, motor-cars. Nevertheless, when the total amount received by the taxpayer as income from real property, capital investments, mortgage debts and the exercise of a profession exceeds 100,000 francs, the tax is assessed on the total of the income from these sources, provided such total exceeds the basic amount of taxation as determined by the application of the indices.

1. TAXPAYERS.

Any individual domiciled or resident in Belgium during the first three months of the year is liable to complementary personal tax if the taxable basis exceeds a legal minimum, varying according to communes and due regard being paid to family circumstances. The tax is payable by anyone who, as owner or tenant, occupies houses or reserves houses for partial or total occupation by his family or servants (seaside villa, country house, shooting-box, etc.).

The tax is not payable by companies, partnerships or legal entities.

2. BASIS OF TAXATION.

The complementary personal tax is assessed on the following bases :

- (1) Rental value of houses ;
- (2) Rental value of the furnishings of houses ;
- (3) Servants and others in the taxpayer's employ ;
- (4) Horses kept for riding and driving ;
- (5) Motor-cars, canoes and steam-launches, motor-boats and yachts, aeroplanes.

Houses. — By houses are meant premises or parts thereof for the private use of taxpayers, including commons, parks or gardens belonging to them, but not including buildings used *exclusively* for the exercise of some profession, trade or industry. The tax is payable by any person who occupies houses or reserves them for occupation, even partially or temporarily, by his family or servants.

¹ *Moniteur* of July 16th, 1930.

The rental value of these houses is the gross income on which the cadastral income is based, ¹ or the actual or presumed income when occupation is limited to part of a house not included separately in the cadastral survey.

Furniture. — The rental value of furniture is fixed at 5 per cent of its capital value as determined by the Law of August 28th, 1921, ² establishing a tax on furniture.

When houses are let furnished, account must be taken of rental value both of the house and of the furniture.

Domestic Servants. — The expenditure index representing the services of domestics and other persons is fixed at :

- (1) 6,000 francs for each out-door worker ;
- (2) 8,000 francs for each maid, sick-nurse or person assimilated to such ;
- (3) 12,000 francs for each male servant ; ³
- (4) 15,000 francs for each tutor, governess, nursery governess, female companion and person discharging similar duties.

Horses. — The index figure in respect of horses used for riding and driving ⁴ is fixed at 12,000 francs per horse.

Carriages, Motor-cars, Canoes and Steamboats, Motor-boats and Sailing Vessels, Aircraft. — The expenditure index applying to these means of transport varies from 2,000 to 50,000 francs, according to rules to be fixed by Royal Decree. ⁵

Division of Indices. — Since the object of the complementary personal tax is that each taxpayer shall pay according to his standard of living, measures have had to be taken to prevent persons dividing their indices with one another and thus unduly benefiting by a reduction of or even exemption from tax. The law therefore lays down that persons living together so as to form one household may not divide their indices. The tax is assessed on all the taxable elements and is payable by the head of the family or the person who occupies the position of head of the household.

Division, however, is allowed between persons who constitute associations having civil personality and not formed for purposes of gain.

3. ASSESSMENT OF TAX.

(a) COMPUTATION OF TAXABLE BASIS AND ABATEMENTS.

Expenditure indices are computed, having regard to the normal situation of the taxpayer on January 1st of the fiscal year.

In the case of persons who become liable to the tax after this date, account is taken of the indices existing on March 31st of the fiscal year.

¹ Gross income is cadastral income plus 25 per cent ; pending the cadastral revision now in process (see note 2 on page 51), the rental values of houses will be the real or presumed rent.

² Amended by Laws of December 31st, 1925, and July 4th, 1930.

³ Male servants include valets, footmen, chauffeurs, coachmen and others performing similar work ; gardeners, keepers and foresters are only placed in this category if they perform personal or household services.

⁴ These include horses kept by persons or families as their own property, hired or reserved for permanent use and used for riding or driving.

⁵ Royal Decree of October 12th, 1930 (*Moniteur* of November 5th, 1930).

The indices once fixed, the taxable basis for complementary personal tax is determined by applying the following coefficients to the total expenditure indices :

- 2 if the total is less than 25,000 francs ;
- 2.2 if the total is from 25,000 to 50,000 francs ;
- 2.4 if the total is from 50,000 to 75,000 francs ;
- 2.6 if the total is from 75,000 to 100,000 francs ;
- 2.8 if the total is from 100,000 to 125,000 francs ;
- 3 if the total is 125,000 francs or more.

Nevertheless, when the total amount received by the taxpayer as income from real property, capital investments, ¹ mortgage debts and professional activities exceeds 100,000 francs, the tax is assessed on the total of the income from these sources, provided such total exceeds the basic amount of taxation as determined by the application of the indices.

For the purposes of carrying out this provision, the income from real property situated in Belgium must correspond to the cadastral income attributed, for the period to which the complementary personal tax refers, to the property which the taxpayer holds on January 1st of the year to which the assessment relates ; as regards income from other sources, the term " income " means that which has been realised during the previous year.

Exempted Minimum. ² — The tax is not due when the taxable basis thus obtained does not exceed :

- 15,000 francs in communes with fewer than 5,000 inhabitants ;
- 20,000 francs in communes from 5,000 to 30,000 inhabitants ;
- 25,000 francs in communes with 30,000 inhabitants or more.

In families with three or more children, this minimum is raised per child dependent upon the taxpayer on January 1st of the fiscal year as follows :

- 2,000 francs in communes with fewer than 5,000 inhabitants ;
- 2,400 francs in communes from 5,000 to 30,000 inhabitants ;
- 3,000 francs in communes with 30,000 inhabitants or more.

Further, the number of out-door workers (*ouvriers-domestiques*) or maids is reduced by one or by two units according as there are, on January 1st of the fiscal year, at least three or at least seven children dependent upon the taxpayer.

As regards seriously disabled ex-servicemen entitled to benefit by the Law of May 13th, 1929, the minima and increases fixed above are further raised up to the amount of the invalidity pension of the person concerned.

(b) COMPUTATION OF TAX AND DEDUCTIONS.

If the minima given above are exceeded, tax is computed on the whole taxable basis.

If the basis does not amount to 25,000 francs, the tax is 1 per cent ; above 25,000 francs, the rate gradually increases for every 25,000 francs or fraction of such amount by $\frac{1}{2}$ per cent up to

¹ Companies other than share companies, but having a legal entity, must file, together with their annual return, a statement indicating under the name of each recipient the amount of the sums allocated or attributed to each member of the company.

If such a statement is not filed, the company is liable to a special tax assessed at 10 per cent of such amount. This tax is assimilated to the complementary personal tax. The payment of the 10 per cent tax by the company dispenses the beneficiaries from declaring, for the purposes of the complementary personal tax, the amounts received.

² The minima and increments may be modified by Royal Decree if there is any change in economic conditions.

125,000 francs, by 1 per cent from 125,000 up to 200,000 francs and by 2 per cent from 200,000 francs up to a maximum of 20 per cent for the part of the taxable basis in excess of 350,000 francs.¹

The complementary tax payable by the head of a family including three children is reduced by 7 per cent for each of these children dependent upon the taxpayer on January 1st of the fiscal year.²

The provinces and communes are not allowed to levy "additional centimes" tax on the complementary personal tax or any similar taxes on the basis or amount of that tax.

4. COLLECTION OF TAX.

The tax is collected on the basis of an annual declaration by the taxpayer and is payable according to the tax list within two months³ of receipt of the assessment notice.

As with schedular taxes on income, persons liable to complementary personal tax may appeal against their assessment to the Director of Taxes (see note 1 on page 51).

¹ Article 7 of the Law of March 23rd, 1932 (*Moniteur* of March 26th), establishes for the years 1932 and 1933 an addition of 10 per cent of the complementary personal tax.

² The deduction so computed may not exceed 2,000 francs for each dependent child (Royal Decree of January 13th, 1933, Article 6).

³ See note 3, page 52.

PART II. — METHODS OF TAXING FOREIGN AND NATIONAL ENTERPRISES.

A. FOREIGN ENTERPRISES.

I. DEFINITION AND GENERAL PRINCIPLES.

If an individual not domiciled or resident in Belgium, or a foreign company whose principal establishment is not situated in Belgium, controls or possesses in the country one or more *establishments*, such establishments are, for purposes of applying the co-ordinated laws on income taxes, deemed to be foreign enterprises.

In principle, a foreign enterprise is liable to schedular taxes only if it has in Belgium one or more establishments dependent upon it. The tax is levied on the total profits from all operations conducted by or through these establishments (Article 27, paragraph 4), the tax on income from land and buildings being imposed only on income from real property situated in Belgium.

I. (a) If income is earned by a foreign enterprise operating in Belgium, but belonging to an *individual*, the whole of the profits realised in the country from all operations conducted by or through the Belgian establishments is liable to tax, which is collected from the owner of the enterprise.

(b) and (c) The same applies when income is earned by a foreign enterprise belonging to a legal entity (*partnership or company*). Only the profits earned by or through Belgian establishments are subject to tax, which is collected from the company or partnership.

On the other hand, if the foreign firm is represented in Belgium by a partnership or company in such a way that the latter in law and in fact directs or conducts operations only on behalf of the said firm, the latter is regarded as having an establishment in the country.¹

If, however, the partnership or company deals in its own name with Belgian customers, selling to or buying from them goods or articles produced by or delivered to the foreign firm, the Belgian company or partnership is regarded as an independent organisation and the Belgian revenue authorities disregard any activities of the foreign firm.

This provision does not, of course, cover cases of fraud or collusion.

II. It follows from the above principles that, if income is earned by a foreign company or partnership having no establishment in Belgium, the company or partnership is not taxable in Belgium on income earned there.

If the enterprise has establishments in Belgium, it does not matter whether income is earned there or not; the foreign enterprise is in any case liable in respect of the total profit resulting from all operations conducted by or through those establishments,² whatever results the general balance-sheet may show.

¹ This contention of the Administration is now before the Courts.

² It has been decided that a foreign company with a Belgian establishment which operates directly in another country must enter in the separate accounts of the establishment all operations conducted in the country, even by agents of the company domiciled abroad.

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) DIVIDENDS.

By virtue of its impersonal character, the tax on income from personal property is imposed on dividends *at the source*, as and when they are received in Belgium and irrespective of the status or nationality of the person presenting the coupons and whether the latter are of Belgian or foreign origin.

Thus in the case of dividends paid by Belgian share companies, tax at 22 per cent¹ is deducted at the source by the body which owes the income, and the beneficiary, whether Belgian or foreign, an individual or a legal entity, and whether domiciled in the country or not, receives the income net.

As regards dividends paid by foreign share companies, whether their head office is in Belgium or not, tax at the reduced rate is withheld at the source by the body paying these dividends in Belgium, unless it is shown that the tax has already been deducted in Belgium by a previous intermediary (Article 23 of co-ordinated laws).

If this dividend is received directly abroad by an individual, company or partnership with a fiscal domicile in Belgium, the amount must be included in the tax declaration which the beneficiary has to make annually to the competent Controller of Taxes. In this case, tax at 6 per cent is levied in accordance with an assessment list and is collected direct from the beneficiary in Belgium (Article 20, paragraph 1, item 4, and Article 50, paragraph 2, of co-ordinated laws).

(b) INTEREST.

Two different cases must be considered :

(1) Interest which a *foreign* firm owes through its establishment in Belgium or to a creditor domiciled in Belgium.

If the foreign firm has an establishment in Belgium which pays the interest, the tax on income from personal property is paid at the full rate of 15 per cent by the debtor company, which, however, may recover the tax on the interest due. Exemption, however, is granted in respect of interest on deposits or debts of a professional character and if it is duly established that the said interest is entered in the accounts of the beneficiary establishments in Belgium.²

If the foreign firm has no establishment in Belgium, the recipient of the said interest, domiciled or resident in Belgium, must mention it in his annual declaration (see *(a)* above) with a view to its assessment to tax at 6 per cent.¹

(2) Interest which a *Belgian* firm owes to a foreign firm.

In this case, tax at 15 per cent¹ is collected by deduction at the time of paying the interest and subject to the right to withhold the tax from the taxable income.

A special regime, however, applies to mortgage interest. Interest from mortgages on real estate situated in Belgium is exempt from tax up to the amount of the cadastral income from such property.

*(c) ROYALTIES FOR USE OF PATENTS AND COPYRIGHTS AND OTHER FORMS OF PERSONAL PROPERTY.**Patents.*

If the patent is simply licensed, personal property tax is deducted at the source by the Belgian debtor at the time of paying the royalty for the licence.

¹ See note 1 on page 54.

² See paragraph (3), page 53.

If the patent is not conceded, but operated by a foreign enterprise direct, the profits from its use are treated as *professional* income and are liable to professional tax on the basis of an annual declaration by the recipient of such income.

Professional tax is applied to subsequent profits from the sale or surrender of a patent when the recipient of the income is domiciled for fiscal purposes in Belgium. The principle of this, however, has been questioned and jurisprudence has not given a definite ruling on the matter.

Copyrights.

These are regarded as professional income and taxed as such. The royalties are received either direct by authors or through special non-commercial associations (*sociétés civiles*) having no legal entity.

In 1928 the revenue authorities entered into negotiations with these companies and it was agreed that professional tax should be collected by them at the time of distributing royalties to authors or their assigns, whatever the nationality of the recipients. For purposes of simplicity, and in order to avoid adjusting the tax to the situation of the innumerable recipients of these royalties, it was decided that the tax should be at a uniform rate of 1½ per cent.

It is paid into the State Treasury at the end of each quarter.

As regards beneficiaries who are neither domiciled nor resident in Belgium, this payment is regarded as final.

Recipients, however, who are domiciled or resident in Belgium are treated like other taxpayers and must include in their annual declaration the amount they have received in royalties. In order to comply with the fiscal requirements, the persons or companies that collect and distribute royalties forward to the revenue authorities at the beginning of the year individual forms for the authors on whose behalf they have paid royalties during the previous year, with the Christian name, surname and domicile of each author and the total amount of royalties paid and tax withheld. On the strength of these forms, the authorities are able to adjust the fiscal position of all those who have to make the annual return. The latter, it should be added, must contain not only royalties paid in Belgium, but those received from abroad.

Royalties received by authors direct without the intermediary of any distributing organisation must, of course, also be included in the annual declaration. ¹

Other Income from Personal Property.

Personal property tax is payable by deduction at source on income from leases and concessions of all personal property.

If the letting of property is in the nature of a business, professional tax is due on the annual profits from these operations.

(d) RENTS FROM REAL ESTATE, MINING ROYALTIES AND SIMILAR INCOME.

The tax, assessed on cadastral income, is levied upon the income from all real estate in Belgium. A foreign enterprise, whether or not it has a Belgian office or business centre where the income is received, is liable to this tax in respect of any real estate it possesses in Belgium.

Income from real estate abroad which is paid in Belgium is liable to personal property tax (note 2, page 50). Accordingly, income of this kind received by the Belgian establishment of a foreign

¹ Under Article 9, paragraph 2 of the Convention concluded between France and Belgium on May 16th, 1931, but which has not yet been ratified, royalties from copyrights and patents are taxable in the country where the recipient is domiciled for fiscal purposes. If, however, they are income from an industrial or commercial enterprise, they are taxable in each country in proportion to the income earned by the permanent establishments there situated.

enterprise (company, partnership or individual), is liable to this tax (at 6 per cent) ;¹ the tax is collected on the basis of the annual return of income.

Mining royalties were abolished in 1925.

On the other hand, a special 10 per cent tax¹ is levied upon the lease of hunting and fishing rights and is payable by the lessees or recipients of such income, provided that the latter amounts to at least 100 francs. The tax is deducted at the source.

(e) GAIN DERIVED FROM THE PURCHASE AND SALE OF REAL ESTATE, PERSONAL PROPERTY AND SECURITIES.

Purchase and Sale of Real and Personal Property.

A foreign enterprise — individual, partnership or company — which has no domicile or establishment in Belgium, but from time to time realises a profit from the purchase and sale of real estate in Belgium, is not taxable on this score. Nor is an individual foreigner who, being domiciled or resident in Belgium, occasionally sells property at a profit. On the other hand, the revenue authorities regard as professional income liable to professional tax on industrial and commercial income any profit of this kind realised in Belgium by a foreign company having an establishment in the country. The reason for this is that, in the case of companies, all operations, even when only occasional, are considered professional.

Purchase and Sale of Securities.

The profit obtained by an individual from the sale of a security bought some time before at a lower price is not regarded as income. On the other hand, profits from speculative transactions by professional speculators, such as stockbrokers, are so regarded.²

In the case, therefore, of stockbrokers and other dealers in stocks and bonds, no difficulty can arise ; all profits from transactions of any kind in securities invested *in their commercial enterprise* must be included in their accounts and figure in the balance-sheet, whether they are cash transactions, dealings for settlement or contango operations.

On the other hand, transactions effected by stockbrokers or dealers in stocks and bonds on their own private account are only taxable if they are *contango* operations or *dealings for a settlement*, these being clearly speculative transactions.

Since any appreciation of the assets of a company is regarded as profit, the tax is payable on all profits—including profits from the purchase and sale, occasional or otherwise, of securities—realised by or through the Belgian establishment of a foreign company.

(f) SALARIES, WAGES, ETC.

Remuneration of this kind paid in Belgium by a foreign enterprise is liable to deduction of professional tax at the source at the official rates. The tax, however, may be remitted on payments to persons whose work on behalf of the Belgian establishment is done entirely abroad. But any expenses of this kind are excluded from the Belgian accounts, the law allowing of no deductions from general overhead or administrative costs except expenses of this kind incurred in the Belgian establishments themselves (Article 27, paragraph 4).

¹ See note 1, page 54.

² Reply by the Minister to a question asked by Senator Beauduin (*Annales Parlementaires*, Senate meeting of June 27th, 1930, page 1204).

(g) INCOME FROM A TRUST.

The case of income from a trust is not provided for by the law, and the revenue authorities have not as yet been called upon to apply the rules to these bodies.

In any case, a distinction must be made according to the nature of the *corpus* of the trust. If it is real estate, tax will be collected on the income from real estate situated in Belgium ; if it is securities or debts, the income therefrom will be liable to tax and deducted at the time the income is paid or, in the case of income paid abroad, in virtue of a declaration. When such income is distributed by the trustee to the beneficiary, it will be regarded as having already been taxed, under Article 52 of the co-ordinated laws, and no further tax will be levied.

(h) INCOME FROM CARRYING ON A BUSINESS OR INDUSTRY THROUGH:

- (1) A local commission agent or broker ;
- (2) A commercial traveller ;
- (3) A local agent with power of attorney ;
- (4) An agent selling out of a stock belonging to the foreign enterprise ;
- (5) A permanent establishment of any kind.

Since a foreign enterprise is taxable in Belgium if it has any kind of *establishment* in the country, there can be no doubt as to the liability of a foreign firm operating in Belgium under the conditions referred to under paragraphs (4) and (5) above.

As explained in Part I, on page 56, the word "establishment" must be understood in a wide sense to include head office, branch, agency, or any public and known representation by authorised agents.

Accordingly, the following have been regarded as establishments of a foreign company : an office employed exclusively in purchasing material and engaging staff for head offices in other countries and in settling the cost of orders and payment of salaries in Belgium ; a local agency of a foreign railway company engaged in selling coupons, subscription books and circular tickets for journeys involving use of the company's lines ; a warehouse for the storage of goods, and a forwarding office possessed in Belgium by a foreign company. Similarly, a foreign firm with subsidiaries in Belgium was deemed to have an establishment in that country when it kept on the premises of those subsidiaries a stock of goods which the company itself insured against fire. A foreign firm is further taxable in Belgium if it has a fixed agent there, whether a depositary or not, who deals on behalf of his principal. Finally, a foreign company is held to have an establishment in Belgium if its name appears on the stationery which its agent uses for his correspondence, or in the form of advertisements, a plate or sign, or in any other manner.

The rules applicable to commission agents and brokers, commercial travellers or agents with power of attorney (paragraphs (1) to (3) above) depend essentially upon the circumstances of the case.

As a general rule, if the commission agent or broker simply takes orders and passes them on to the foreign firm, without intervening in any way in the transactions between the firm and its customers (delivery of goods, payment of invoices, judicial disputes, etc.), the revenue authorities consider that there is no Belgian establishment and the foreign firm is therefore not liable to tax on profits derived from the orders thus received. The commission agent or broker must not mention the firm he represents on his stationery or by any plate or sign at his premises.

The operations of a foreign commercial traveller in Belgium do not of themselves constitute an *establishment* justifying the taxation of the foreign firm. Subject, however, to exceptions provided for in international conventions, such traveller is liable to a minimum professional tax of 200 francs, which he has to pay before carrying on his business in Belgium (Article 27, paragraph 4, (3) and (4)).

On the other hand, an agent with a power of attorney which allows him to engage the name of

the foreign enterprise, to participate in the delivery of goods and the collection of payments, to take judicial action on behalf of the enterprise, etc., is deemed to constitute a foreign establishment, the activities of which are assessable to tax.

B. NATIONAL ENTERPRISES.

For the purpose of this study, a national enterprise is one whose domicile, in the case of an individual, or head office or principal establishment, in the case of a company or partnership, is in Belgium.

Such enterprise is taxable in Belgium, not only on *all profits* earned in the country, but on those earned abroad; the latter, however, are taxed at reduced rates (Article 34, paragraph 1, item 4, and article 35, paragraph 7, of co-ordinated laws) and are exempt from additional tax by provinces and communes.

Tax is assessed on the total results of the enterprise (Belgian and foreign offices), which means that profits and losses are balanced against each other, so that, if the total operations result in a deficit, no tax is payable.

To ensure the execution of these legal provisions, national enterprises have to attach to their annual declaration, not only the general accounts, but a copy of the separate balance-sheet and profit-and-loss account of the foreign establishments (Article 54, paragraph 1 (3), of the laws above-mentioned). These separate accounts include all income, of any kind whatever, derived from foreign sources.

TAXATION OF CERTAIN KINDS OF INCOME.

(a) DIVIDENDS.

The tax on income from personal property is levied at the rate of 6 per cent¹ on foreign dividends received by the Belgian company; the tax is deducted *at the source* by whoever pays this income in Belgium. If it is paid directly abroad, it must be mentioned in the annual return made by the enterprise to the competent Controller of Taxes, who then collects tax at 6 per cent direct from the company.

(b) INTEREST.

Interest (on bonds, debts, deposits, loans, etc.) from a foreign source is also liable to tax on income from personal property at 6 per cent, according to the method mentioned under (a).

(c) to (h) INCOME OTHER THAN DIVIDENDS AND INTEREST.

See what has been said above (pages 69 *et seq.*) in connection with foreign enterprises, noting, however, that the income in question is taxable at reduced rates if earned and taxed abroad.

If the national enterprise is directed by an individual, professional tax alone is due, a reduced rate being applied to that part of the tax corresponding to profits earned and taxed abroad.

In the case of partnerships, the legal entity is liable to professional tax on profits placed to reserve, income of foreign origin being taxed at a lower rate than income of Belgian origin. Active partners are liable to professional tax on the sums distributed to them, including any interest on capital they have invested in the partnership. A reduction of rate is allowed in respect of parts of these sums which represent profits taxed and earned abroad. Sleeping partners (*baillieurs de fonds* or *commanditaires*) pay tax on income from personal property, subject to the same reduction of rate on foreign income.

¹ See page 54, note 1.

The same principle (reduction of rate) applies to profits placed to reserve by share companies (*sociétés anonymes*) and limited partnerships with share capital (*sociétés en commandite par actions*); in the case of distributed profits (dividends), personal tax is imposed at a reduced rate on that proportion of income from shares corresponding to profits earned and taxed abroad.

C. TREATY PROVISIONS.

I. GENERAL REMARKS.

Belgium has concluded bilateral Conventions for the avoidance of double taxation with the Grand-Duchy of Luxemburg, France and Italy. Ratifications have so far been exchanged with the Grand-Duchy and Italy.

The texts of these Conventions are not uniform, for the fiscal systems of the four contracting States are in certain respects so different that no one solution could be found wholly acceptable to each of them.

Nevertheless, the provisions are substantially the same as far as concerns liability to tax on income from land and buildings, the taxation of the income of industrial, mining, commercial or agricultural enterprises, income from labour, fees of directors and auditors of share companies, public and private pensions and annuities.

The taxation of income from securities is not dealt with in the Convention with the Grand-Duchy of Luxemburg owing to fundamental differences in the fiscal treatment of such income by the two countries. It was omitted from the Convention with Italy because the interests affected are of very secondary importance. On the other hand, the question has been amply treated in the and private Convention with France.

DEFINITION OF FISCAL DOMICILE.

The Conventions define fiscal domicile as follows: The fiscal domicile of individuals is the place where they normally reside — that is, where they have a permanent home. Companies and partnerships having a separate legal entity are domiciled for fiscal purposes in the place where they have their real head office; the fiscal domicile of other legal entities is their real centre of direction or management.

From the standpoint of Belgian law, therefore, the conception that determines the fiscal domicile of individuals is residence (see page 49); in the case of companies and partnerships with a separate legal entity, the determining factor is their *real* head office, which is usually synonymous with the principal establishment as laid down by Belgian fiscal law. The real centre of direction or management, constituting the fiscal domicile of other legal entities, likewise coincides with the principal establishment as understood by Belgian jurisprudence.

From this point of view, the Conventions do not introduce any essentially new principle into co-ordinated Belgian law.

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) DIVIDENDS.

In principle, the Belgian tax on income from personal property is collected from dividends at the source at the full or reduced rate according to their Belgian or foreign origin.

The Conventions with France and Italy provide that income from shares and similar forms of participation shall be taxable in the country where the real head office is situated.¹

¹ The Conventions even extend this treatment to income from interests in limited partnerships and from shares in non-commercial and limited liability companies (*sociétés civiles et à responsabilité limitée*).

As an exception, however, to this rule, the Franco-Belgian Convention prescribes that income from securities (public debentures, shares or other certificates issued by companies, bonds or other loan scrip) is liable to impersonal tax in the State where the beneficiary has his fiscal domicile, to be collected according to the laws of that country. In this case, however, the State will deduct from this tax the tax already paid on the same income in the other country.

In view of the present incidence of taxation in France and Belgium, it was agreed that this provision should be applied as follows :

As regards Belgium, and in so far as the general tax rate on income from foreign securities does not exceed 12 per cent,¹ this tax will not be payable on income from French securities accruing to persons having their fiscal domicile in Belgium. Should the general rate exceed 12 per cent, it will be reduced by 12 per cent in respect of these securities. As regards France, the general rate of the tax on income from foreign securities will be reduced by 12 per cent in the case of Belgian securities.

Further, French share companies having their fiscal domicile in France and a permanent establishment in Belgium may, when making their annual return in Belgium, apply to be treated like Belgian share companies ; in this case, the tax on dividends is assessed on a fraction of the Belgian profits equal to the ratio between the distributed profits of the company and its total profits, provided, however, that the sum assessable to the taxes on professional and personal property income does not exceed the total Belgian profits.

A French company which asks for this treatment will have to pay : (i) the tax on income from personal property at the full rate applying to share income on the portion of Belgian profits determined by the above-mentioned ratio ; (ii) professional tax at the ordinary rates on the remainder of those profits, whereas, at present, the whole of the taxable profits earned in Belgium are liable to professional tax at 10 per cent.

At the same time, the total income liable to personal property and professional income taxes may not exceed the Belgian profits.

(b) INTEREST.

Under ordinary law, personal property income tax is payable in Belgium, by deduction at source or on an annual return, in respect of all interest paid or received by a person who has his domicile or residence in Belgium.

The Conventions concluded with France and Italy depart from this principle when they lay down that income of this kind is taxable in the country where the person owing the income is situated; no attention is thus paid to the domicile of the recipient.

If, however, the debtor has permanent establishments in both countries and if one of these establishments contracts a loan or receives a deposit in the strict course of its business, the tax is collected by the State in which the establishment is situated.

(c) COPYRIGHT ROYALTIES.

Under the Conventions, copyright royalties are taxable in the country where the beneficiary has his fiscal domicile.

Consequently, professional tax can no longer be collected in respect of copyright royalties paid in Belgium to persons whose fiscal domicile is in the Grand-Duchy, France or Italy.

(d) RENTS FROM REAL ESTATE, MINING ROYALTIES AND SIMILAR INCOME.

Contrary to the rule of Belgian fiscal law, whereby income from real estate received abroad by a person domiciled or resident in Belgium is liable to personal property tax, the Conventions concluded

¹ At present it is 6 per cent plus an additional tenth (*décime additionnel*).

with the Grand-Duchy of Luxemburg, France and Italy provide that the income from real property, or the property itself, is taxable only in the State where the property is situated.

(e) SALARIES AND WAGES.

Normally, remuneration paid in Belgium, including the fees of directors of share companies, is subject to deduction of professional tax at source ; further, remuneration received abroad by a person domiciled or resident in Belgium is liable to professional tax on the basis of an annual declaration. The tax, however — which is fixed by the Belgian commune where the taxpayer is domiciled or resident — is computed at a reduced rate if the income is earned and taxed abroad.

The Conventions lay it down as a rule that the fees of company directors and of others discharging similar functions are taxable in the State in which the enterprise has its real head office.

The various payments to salaried workers and wage-earners are taxed in the country in which the taxpayer is working.

The salaries of the public servants of one country who exercise their functions in the other are taxed only in the country which pays them.

Finally, public and private pensions are taxed in the country which owes this income, annuities in the country in which the recipient has his fiscal domicile.

Accordingly, tax will in future be collected, in respect of the income mentioned above, by one State only : in the case of directors, etc., of share companies, by the country in which the enterprise has its real head office ; in the case of salaried workers and wage-earners, by the country where they do their work ; in the case of public servants, by the country which pays them ; in the case of pensions, by the country which owes them and, in the case of annuities, by the country in which the recipient has his fiscal domicile.

(f) INCOME FROM THE CARRYING-ON OF A BUSINESS OR INDUSTRY.

National Enterprises operating abroad.

According to Belgian law, a *national* enterprise which has establishments abroad is liable to tax in respect of all its Belgian and foreign profits, but profits earned and taxed abroad are taxed in Belgium at a reduced rate.

Under the Conventions, industrial, mining, commercial and agricultural enterprises are taxable in each State only in proportion to the income earned by *permanent* establishments therein.

This is a modification of the Belgian regime, since it exempts from tax in Belgium profits realised in the Grand-Duchy, France and Italy by Belgian enterprises which have establishments in those countries.

Foreign Enterprises deriving Income from Belgian Sources.

It was explained on page 56 that a foreign enterprise is taxable in Belgium if it has any kind of " establishment " in that country, the term " establishment " being interpreted in a very wide sense to cover anything between a centre of operations and some recognised public representation by authorised agents.

The Convention concluded by Belgium with the Grand-Duchy of Luxemburg restricts the term to somewhat narrower limits. By *permanent* establishment are to be understood centres of effective management, branches, factories, workshops, agencies, shops, offices and dépôts. The fact that

an enterprise established in one of the two contracting States maintains business relations with the other country through a really independent agent or company (broker, commission agent, subsidiary, etc.), does not imply that the enterprise has a permanent establishment in the latter country.

Subject to this same reservation, the Conventions concluded with France and Italy define the term "permanent establishment" so as to include purchase and sales offices and any other fixed installation of a productive character. On the other hand, the Convention with France provides that offices which merely buy goods to supply them to one or more selling or processing establishments of the enterprise in the other country shall not be taxable — subject, of course, to reciprocity.

3. PROVISIONS RELATING TO THE COMPLEMENTARY PERSONAL TAX.

The question of complementary tax did not arise in connection with the Grand-Duchy of Luxemburg, which has no such separate impost. Nor was it dealt with in the Franco-Belgian Convention.

The Convention with Italy, however, lays down that a taxpayer is liable to complementary tax only in the country where he has his fiscal domicile.

If a person domiciled in Italy has a second residence in Belgium, he is fiscally domiciled in both countries, and the Convention provides that in that event he would be liable to complementary tax in Belgium in proportion to the length of his visits to that country, whereas, under Belgian law as it now stands, personal tax would be due for the whole year.

PART III. — METHODS OF ALLOCATING TAXABLE INCOME

A. FOREIGN ENTERPRISES WITH LOCAL BRANCHES OR SUBSIDIARIES.

I. GENERAL QUESTIONS AND METHODS OF APPORTIONMENT.

Under existing fiscal law, foreign firms are taxable on profits resulting from any operations conducted by or through their Belgian establishments.

Subsidiaries are generally regarded as separate and independent legal entities and are therefore subject to the fiscal regime of the Belgian companies whose form they have adopted. They are thus liable to income-tax in accordance with the statements in their own accounts, which have to mention separately the results of their Belgian and foreign operations, for the purpose, more particularly, of applying a reduced rate of taxation to profits earned and taxed abroad (see page 56).

The question of allocation arises therefore only as regards branches of foreign enterprises.

(a) BOOK-KEEPING AND ACCOUNTING REQUIREMENTS.

In principle, a foreign firm which has a branch in Belgium must itself declare the income earned by the establishment and in support of its annual return must produce the separate accounts of that establishment referred to in Article 27, paragraph 4, second sub-section.

These accounts are not specified in detail in the fiscal law ; they may consist of the day-book and other books commonly used in business and the use of which is prescribed in Article 16 of the Law of December 15th, 1872 (Commercial Code).¹

In any event, the separate accounts must permit of the drawing up and checking of the separate balance-sheet and profit-and-loss account relating to business done by the establishments, or a summarised statement showing by classes the various operations conducted by these establishments and the total profits resulting therefrom.²

Should such accounts not be kept or should the results not be produced, or if the revenue authorities have serious reason to believe that the accounts do not reveal the real results of operations, the profits of the foreign establishment may be determined either empirically or by the method of comparison provided for in Article 28 of the co-ordinated laws.

¹ Every trader has to keep a day-book, in which he enters daily his assets and liabilities, trading operations negotiations, acceptances and endorsements of bills and, in general, all kinds of receipts and payments. The book must further contain a monthly statement of all household expenses — all this apart from other books commonly used in business, but the keeping of which is not compulsory (Article 16 of Law of December 15th, 1872, Commercial Code).

² Accounts kept abroad by a foreign firm carrying on business in Belgium do not comply with the requirements or the purposes of Article 27, paragraph 4. Judgment rendered by the Brussels Court of Appeal, November 7th, 1931.

When accounts, the truth and accuracy of which are above question, or accompanied by the necessary supporting data, are not produced, the Administration is entitled to proceed to an arbitrary assessment. Judgment rendered by the Brussels Court of Appeal, January 21st, 1933.

(b) METHODS OF ALLOCATION.

I. *Method of Separate Accounting.*

The separate accounts of the branch must include all operations transacted in Belgium by or through the branch. It does not matter whether the business is done with persons in the country or with foreigners. Nor does it matter whether the operations are initiated by the Belgian establishments or are simply conducted through their agency. The operations will in both cases be entered to their account for purposes of determining the profits earned in Belgium.

The accounts will include, for instance, interest received in Belgium and profits from the investment of money by the Belgian branches at the direct orders of the head office.

On the other hand, the only deductions allowed under general or administrative costs of the Belgian establishments are expenses of this kind incurred by the said establishments.

Deductible expenses do not include interest, premiums or prizes paid by the said establishments to bond-holders, nor fees paid to directors and auditors out of the profits earned in Belgium — except when schedular taxes have been paid under this head in Belgium.

2. *Empirical Methods.*

In the absence of exact allocation evidence derived from accounts kept in accordance with the Commercial Code, or documents confirming with sufficient accuracy the income declared, foreign firms operating in Belgium are taxed on a certain *minimum* profit, fixed as explained below, the tax, however, being not less than 10,000 francs (Royal Decree of October 8th, 1930, ¹ issued in execution of Article 28 of the co-ordinated laws) :

- (1) Factories, workshops, building works, quarries, brickyards and tile-works, railway works : 3,000 francs per employee and workman (average number for year in question) ;
- (2) Agricultural undertakings : empirical scale laid down for farmers in the neighbourhood ;
- (3) Horticulture or market-gardening : four times the cadastral income of the exploited property ;
- (4) Banks, credit and exchange institutions : 15,000 francs per employee (average number for year in question) ;
- (5) Life insurance : 20 francs per 1,000 francs of received premiums ;
- (6) Maritime insurance : 25 francs per 1,000 francs of received premiums ;
- (7) Other insurance : 60 francs per 1,000 francs of received premiums ;
- (8) All other enterprises, etc. : 150 francs per 1,000 francs of receipts, with a minimum of 10,000 francs per employee and workman.

The separate accounts can, of course, be checked by the revenue authorities, who are in no way bound by the information in them. As in the case of the balance-sheets of Belgian enterprises, ² this control may consist in demanding explanations and further evidence whenever the fiscal agents think fit. This applies especially to the prices at which goods have been invoiced by the parent enterprise to its branch or subsidiary. If the Controller has reason to believe that these prices are higher than those invoiced by similar enterprises or those officially quoted, he may disregard the figures in the accounts. In this case, the presumed additional profit is added to that shown in the accounts ; or, if the figures are altogether unreliable, the authorities may wholly disregard them and assess tax *ex-officio*. ³

¹ *Moniteur* of October 19th, 1930.

² Judgments of the Court of Cassation, March 19th, 1894 ; of Brussels Court of Appeal, February 5th, 1904 ; see also note 2, page 78.

³ The competent courts are now being asked to decide upon the merits of *ex-officio* assessment in these circumstances.

The same care is needed when the separate accounts contain mention of interest on loans and advances paid to the parent enterprise, or of sums due for management or engineering service, use of patents, etc.

As regards interest on loans and advances, the only deduction allowed under the heading of professional charges (Article 26, paragraph 2, of the co-ordinated laws) is interest on capital borrowed from third parties and invested in the business ; since the branch does not constitute a third party *vis-à-vis* the parent firm — the head office and Belgian branch being two parts of one organisation — the revenue authorities include this interest among the profits of the Belgian establishment.

Sums paid for management and engineering service imply the exercise by the parent enterprise of activities in Belgium, and the revenue authorities levy professional tax on the foreign enterprises in respect of the net profit from these activities.¹

Lastly, royalties paid to the parent enterprise for the lease, concession or use of patents come under Article 14, paragraph 4, of the co-ordinated laws, by which the total amount is assessable to personal property income tax.

The revenue authorities are not, however, bound exclusively to the empirical method ; they may also fix the taxable income by a method of comparison, regard being had to the normal profits of taxpayers similarly situated and, as the case may be, to invested capital, turnover, number of workmen, motor-power used, rental value of exploited land and any other useful information (Article 28 of the co-ordinated laws), should this method seem more likely to reveal the true facts. In practice, however, the empirical method is the normal substitute for accounts ; recourse to the comparative method is exceptional.

The criteria on which the latter method is based are the *bona-fide* declarations of taxpayers who keep regular accounts and operate under similar conditions. The law does not prescribe any particular element of comparison (invested capital, turnover figure, number of workmen, etc.). This is left to the discretion of the fiscal agents, provided only that the method employed shall succeed in fixing as closely as possible the presumed profits on which tax is to be assessed.

3. *Method of Fractional Apportionment.*

If the company fails to produce reliable accounts and should the application of the empirical or comparative method not be thought satisfactory, the taxable income may also be determined as a fraction of the total income of the foreign company. In this case, the latter is required to furnish the revenue authorities with the general accounts of the enterprise and all other information necessary to assess tax on an equitable basis. There are no express administrative provisions to this effect, but the general purpose is to harmonise as closely as possible the various documentary evidence at the disposal of the fiscal agents.

The question really only affects foreign companies operating in Belgium through a branch, as subsidiaries mostly have a separate legal existence involving taxation on their own account.

4. *Requirements for Selection of Methods and Relative Value of the Various Methods.*

In principle, allocation is based upon the taxpayer's declaration, supported by the separate accounts² and subject to checking by the revenue authorities. If there are no special accounts or if they are not sufficiently trustworthy, allocation may be made empirically. The empirical or comparative method is only used if there are special reasons for doing so and if the taxpayer agrees to it.

¹ Judgments of Brussels Court of Appeal, dated March 29th, 1929, and July 2nd, 1932.

² See note 2, page 78.

The most practical and satisfactory method is taxation in accordance with accounts susceptible of being verified by the Administration. If it cannot be employed, an empirical method offers an alternative solution, although it is not always in accordance with the facts.¹

In actual practice, however, the revenue authorities are satisfied with any method of assessment which will furnish as exact an estimate as possible of the profits earned by a foreign firm in Belgium.

(c) APPORTIONMENT OF PROFITS BETWEEN BRANCH AND PARENT ENTERPRISE.

1. *Apportionment of Gross Profit of Local Branch to Real Centre of Management abroad.*

When assessing the profits derived from operations carried on in Belgium, no fraction of these profits is attributed to the real centre of management abroad.

As explained above (page 78), tax is assessed in Belgium upon the profit from all operations conducted in the country by or through the Belgian establishments, the only deduction allowed being the professional expenses of the Belgian office. The Belgian establishment is considered separately for the purpose of determining profits and therefore none of these are ascribed to the real centre of management abroad.

2. *Apportionment of Expenses of Real Centre of Management to Branch.*

Interest Charges.

Jurisprudence has decided that, in the case of Belgian enterprises which earn profits abroad, interest charges are ascribed to the head office. The only exception is when the debt has been contracted abroad on behalf of establishments situated abroad.

Applying this jurisprudence, the revenue authorities consider that the interest payable on a general debt of a foreign enterprise is ascribed to the real centre of management, unless it is clearly established in law that the debt was contracted in Belgium by the Belgian establishment for its own requirements; in the latter case, the interest is liable to personal property income tax in Belgium.

General Overhead.

As regards foreigners operating in Belgium, the only general overhead or administrative expenses which may be deducted are expenses of this kind incurred by the Belgian establishments (Article 27, paragraph 4, of co-ordinated laws).

Deductible expenses — subject to what was said above about interest charges — do not include interest or premiums paid by these establishments to bond-holders, or fees paid to directors and auditors out of profits earned in Belgium.

If there is any doubt as to the accuracy of general overhead or administrative expenses as shown in the accounts, details are asked for.

3. *Apportionment of Net Profit of Branch to Deficitary Parent and vice versa.*

Foreign enterprises are taxed on the profits from all operations conducted by or through their establishments in Belgium. No regard need therefore be had to any loss in the results of the entire enterprise; none of this loss can likewise be ascribed to the separate accounts of the Belgian branch.

Applying the above principles, the taxable basis is fixed with exclusive regard to the results of the Belgian establishment. If the separate accounts reveal a loss and are found by the fiscal agents

¹ The method used the first year must be adhered to; the taxpayer is not allowed to choose the empirical method one year and to be taxed on the basis of accounts the next year.

to be in order, no tax will be levied in Belgium, even though the entire enterprise should realise a profit.

(d) APPORTIONMENT BETWEEN PARENT ENTERPRISE AND SUBSIDIARIES.

There is no apportionment of profits between parent branch and subsidiary, the latter being regarded in Belgium as independent and liable in respect of all its profits to fiscal rules of its own.

II. APPLICATION OF THE METHODS OF ALLOCATION IN SPECIFIC CASES.

(a) INDUSTRIAL AND COMMERCIAL ENTERPRISES.

I. *Selling Establishments.*

Local Establishments selling in National Markets.

In principle, a foreign establishment in Belgium has to keep separate accounts of its Belgian operations. If the results shown by these accounts are accepted, assessment is on this basis, but, if not, recourse will be had to one of the methods referred to under "General Questions and Methods of Apportionment".¹

The profit from sales may be determined (in Belgian francs) by deducting from the sale price : (a) the value of the goods at the time they were consigned to Belgium ; (b) the cost of transport to Belgium including insurance and import duties ; (c) costs of handling, storage, warehousing or packing in Belgium prior to sale ; (d) other general expenses in Belgium in connection with these operations.

In principle, the production of the original sales invoices allows the fiscal agent to satisfy himself that these prices are normal having regard to the prices of the same goods produced in Belgium. In the case of special articles without any known current price, the Controller may refuse to accept the accounts if he has reason to doubt their accuracy ; in this case assessment will be on an empirical basis.

Local Establishments selling abroad.

Profits derived from sales to customers abroad are all ascribed to the branch in Belgium, when the sales were effected through that branch. The law does not prescribe what part the Belgian establishment must play in order that it may be regarded as the agent of sale. In practice, all operations are ascribed to the branch which are concluded by it with the third State, even if they required the authorisation of the real centre of management.

2 and 3. *Manufacturing and Processing Establishments.*

No legal provision ascribes to a manufacturing establishment a given part of profits from the sale abroad of goods manufactured in the country. The revenue authorities have to examine in each case whether and to what extent the manufacturing establishment is to be regarded as having earned profits in Belgium.

4. *Buying Establishments.*²

In principle, a permanent establishment situated in Belgium has to keep separate accounts of all operations conducted in the country, including purchases made on behalf of the

¹ A foreign firm possessing in Belgium a branch managed by a proxy, at which centre all the sales and eventually the purchasing of cereals were undertaken by this official under direct instructions from the company, was judged taxable there. Judgment of the Brussels Court of Appeal, February 18th, 1933.

² The tax liability of buying establishments and of forwarding agents has been established by judgment of October 31st, 1932, of the Court of Cassation.

principal enterprise. Assessment is based either on these accounts or on one of the methods already mentioned.

The foreign enterprise is not taxable if purchases are made from a local subsidiary, which, being regarded as an independent company, is taxed on the whole of its profits.

5. *Research or Statistical Establishments, Display Rooms, etc.*

Profits could be ascribed to establishments of this kind in Belgium, on the principle that a foreign enterprise is taxable if it has an *establishment* in Belgium. The revenue authorities have decided that a foreign company wishing to establish an office for supervision and control in Belgium shall be deemed to have an establishment there. If, however, the separate accounts show no profits and, on being produced, are accepted as being in order, no tax is levied.

(b) BANKING ENTERPRISES.

No special method of assessment is used for these institutions. Their income is determined either on the basis of their separate accounts, if approved, or empirically; the latter method prescribes for these enterprises a minimum taxable profit of 15,000 francs per employee, taking the average number of employees for the year in question.

The revenue authorities are not aware of any case in which the comparative method has had to be used.

(c) INSURANCE ENTERPRISES.

In principle, profits are determined from the separate accounts. It may be remembered (see page 60) that these accounts are not required to show profits separately according to the class of contract (life insurance, temporary, mixed, etc.), but only according to the branch of insurance (life, fire). On the other hand, the separate accounts must include: the gross premiums (see note 3 on page 60) collected by the Belgian agencies without deducting premiums surrendered to reinsurance companies; the reserves corresponding to policies concluded by these agencies or contracted in Belgium by agents domiciled abroad; interest on these premiums and reserves; compensation paid by the Belgian agencies; the latter's general expenses; and, lastly, reinsurance operations relating to policies concluded by the Belgian agents or contracted in Belgium by agents domiciled abroad, etc.

For purposes of uniformity, the Administration has prescribed the production of a standard profit-and-loss account containing all the information required.

In the absence of properly kept accounts, or if such are not produced, the empirical method is employed, with the following minimum profits:

Life insurance: 20 francs per 1,000 francs of paid premiums;

Maritime insurance: 25 francs per 1,000 francs of paid premiums;

Other insurance: 60 francs per 1,000 francs of paid premiums;

The comparative method has not as yet had to be applied.

(d) TRANSPORT ENTERPRISES.

Same as for (b). Under the empirical method, however, the minimum taxable profit is 150 francs per 1,000 francs of receipts, but not less than 10,000 francs per employee and workman; in the case of railways, the minimum is 3,000 francs per employee and workman (average number for year in question).

The Government is authorised to conclude international agreements granting, subject to reciprocity, complete fiscal exemption to the income of foreign shipping enterprises domiciled in Belgium. Agreements of the kind have been concluded with Norway, Denmark and Iceland, Finland, Ecuador, Sweden and France, and negotiations are proceeding with other countries.

(e) POWER, LIGHT AND GAS ENTERPRISES.

Same as for *(b)* ; if the empirical method is used, the minimum profit is 150 per 1,000 francs of receipts, but the taxable income must be not less than 10,000 francs per workman and employee.

(f) TELEGRAPH AND TELEPHONE ENTERPRISES.

In Belgium, telegraphs and telephones are operated by a Government monopoly, which is not taxable.

(g) MINING ENTERPRISES.

Same as for *(b)* ; the empirical method assumes a minimum profit of 3,000 francs per employee and workman (average number for year in question).

(h) ANY OTHER KIND OF ENTERPRISE REQUIRING SPECIAL TREATMENT.

Same as for *(b)* ; the empirical method presupposes a minimum profit of 150 francs per 1,000 francs of receipts, with a minimum taxable income of 10,000 francs per workman and employee.

B. NATIONAL ENTERPRISES WITH BRANCHES OR SUBSIDIARIES ABROAD.

I. GENERAL METHODS OF ALLOCATION.

National enterprises which make profits from separate establishments abroad have to attach to their annual declaration a copy of the separate balance-sheets and profit-and-loss accounts of these establishments (Article 54, paragraphs 1, (3), 2).

For the rest, reference may be made to page 60 " National Enterprises operating abroad " .

II. ALLOCATION OF PROFITS TO REAL CENTRE OF MANAGEMENT WITHIN THE COUNTRY.

In this matter, the revenue authorities rely upon the accounts, if these appear to be in order, and if the accounts show that all the profits are of foreign origin, the law forbids any part of them being ascribed to the real centre of management.

C. HOLDING COMPANIES.

I. NATIONAL HOLDING COMPANY CONTROLLING ONE OR MORE FOREIGN SUBSIDIARY.

Holding companies, like companies with their head office or principal administrative establishment in Belgium and separate establishments abroad, have to keep accounts of the income they derive from both Belgian and foreign sources. Dividends and interest paid in Belgium are liable to deduction of personal property income tax at the source at full or reduced rate, according as the income is of Belgian or foreign origin. In the case of foreign income paid abroad, the holding company has to declare it and pay personal property income tax on it at reduced rate.

Since such income, both Belgian and foreign, must not be taxed twice, the profits of these companies corresponding to the net dividends they receive may be used to build up or add to their reserves, or may be distributed to the shareholders of the company, without payment of any further tax.

The same rule applies to debenture interest and coupons on bonds or to other interests. If this income has paid personal property income tax, its net amount is not liable to further tax when included among profits placed to reserve or distributed.

II. LOCAL SUBSIDIARY CONTROLLED BY A FOREIGN HOLDING COMPANY.

In conformity with the principles explained in Part I, local subsidiary companies are taxed on their total profits both Belgian and foreign, those earned in Belgium being taxed at full rate, those made abroad at a reduced rate. The local company pays the personal property income tax for which it is liable when it pays its dividend, so that the foreign holding company receives income on which Belgian tax has been duly paid. At the same time, the holding company itself is not regarded as liable to tax in Belgium, since it has neither its head office nor its chief administrative establishment in the country.

D. TREATY PROVISIONS.

I. NATIONAL ENTERPRISES OPERATING ABROAD.

In principle, a taxpayer who has his head office or principal establishment in Belgium and other establishments abroad is taxed on the whole of the profits earned in Belgium and abroad. Tax is assessed on the basis of the general balance-sheet and of the special profit-and-loss accounts relating to the business of the separate foreign establishments, the foreign profits being taxed in Belgium at a reduced rate if already taxed abroad.

According to the Conventions concluded with the Grand-Duchy of Luxemburg, France and Italy, industrial, mining, commercial and agricultural enterprises are taxable in each country in proportion to the income earned by the permanent establishments therein.

This procedure constitutes a departure from the normal rule. The Belgian authorities will therefore no longer tax the profits of establishments in the Grand-Duchy, France and Italy, but the profits of establishments situated in other non-contracting States will continue to be subject to ordinary Belgian law.

Allocation will be based on regular accounts. If there are no regular accounts showing the income separately and accurately, the competent authorities of the contracting States will, if need be, agree upon certain rules of apportionment.

II. FOREIGN ENTERPRISES DERIVING INCOME FROM BELGIAN SOURCES.

In this matter, the Conventions make little change in Belgian fiscal law : the foreign enterprises will be taxable in Belgium only if they have a permanent establishment there. The tax will be assessed exclusively on profits earned in Belgium by or through the said establishment, and these profits will not be taxed in the other country.

The Convention with Italy, however, prescribes that the profits of shipping and air navigation companies, including profits from the sale of tickets, shall be taxable only in the country in which the enterprise has its real head office, provided that the vessels or aeroplanes belong to that State.

Annex.

TABLE OF TARIFFS.

I. LAND-TAX (TAX ON INCOME FROM LANDED PROPERTY).

Seven per cent of cadastral income, plus additional centimes levied on behalf of the provinces and communes at varying rates according to the localities.

II. TAX ON INCOME FROM PERSONAL PROPERTY.¹

A. *Income of Belgian Origin:*

	Percentage rate of tax
1. Income from shares in commercial or non-commercial companies and partnerships having their head office or principal administrative establishment ² in Belgium, except as provided in No. 11 below ³	22
2. Income from bonds or other debts incurred by the companies or partnerships mentioned in No. 1, except as provided in No. 13 below ³	15
3. Income from debts ⁴ incurred by individuals or companies and partnerships other than those mentioned above	15
4. Income from deposits ⁴ other than those specified under Nos. 8 to 11 below.	15
5. Income from the rent, lease, use or concession of all personal property (but see, as regards hunting and fishing rights, letter D below)	15
6. Income from capital invested in companies, other than share companies, by sleeping partners	10 ⁵

¹ Article 7 of Law of March 23rd, 1932 (*Moniteur*, of March 26th), fixes, for 1932 and 1933, an additional 10 per cent on the personal tax; the rates indicated should be therefore increased by 10 per cent during those years. As regards tax on income of foreign origin paid abroad, this additional 10 per cent is only levied on the tax on income paid after April 1st, 1932.

² Dividends, interest, total or partial repayment of corporate capital and taxable sums distributed in the event of a division of the company's assets, except the part corresponding to profits earned and taxed abroad (see No. 12).

³ There are, however, special rules for colonial companies (Law of June 21st, 1927); see page 54.

⁴ Except professional debts or deposits, provided the taxpayer can satisfy the Administration that the interest thereon is included in the accounts of the Belgian beneficiary establishment and therefore, to that extent, swells the taxable profits of the latter.

⁵ Plus additional tax on behalf of provinces and communes.

	Percentage rate of tax
7. Income from bonds issued by the Belgian State, the provinces, communes and other public bodies ¹ and from debts incurred by them.	2
8. Income from deposits with the <i>Caisse générale d'Épargne et de Retraite</i> and the <i>Caisse des Dépôts et Consignations</i> ²	2
9. Income from deposits with other public savings banks ^{2 3}	2
10. Income from loans granted after July 1st, 1932, to agricultural or commercial enterprises which have their seat in Belgium, provided it is shown that such loans were specially intended to provide employment ⁴	2
11. Income from deposits with private savings banks satisfying certain conditions ^{2 3 5}	5

B. Income of Foreign Origin or Income assimilated thereto.

12. Income from shares, referred to in No. 1, in a proportion corresponding to profits earned and taxed abroad ⁶	6
13. Income of foreign origin other than that mentioned above (income from foreign shares or bonds, foreign State funds, foreign debts, foreign deposits, real estate situated abroad, etc.).	6
14. Income from bonds issued abroad for the needs of foreign establishments ⁷	5
15. Income from sums of money deposited in Belgium by individuals or legal entities having no domicile, residence or establishment in the country ⁸	5

¹ Exemption is granted to bonds issued prior to January 1st, 1919, by the State, provinces and communes. Further, income from the following State funds enjoys special exemption :

- (a) Interest on the National Reconstruction Internal Loan (Law of March 16th, 1919) ;
- (b) Interest and redemption premium on loans issued abroad (Laws of March 16th and October 24th, 1919) ;
- (c) Interest and redemption premium on the 5% Premium Loan (Law of January 27th, 1920) ;
- (d) Interest and redemption premium on the 6% Loan issued in Belgium by the Grand-Duchy of Luxemburg (Article 4, Law of July 12th, 1922) ;
- (e) Interest on the Belgian Congo Debt : 2½ per cent, 1887; 4 per cent, 1896-1898; 4 per cent redeemable 1901; 3 per cent, 1904 (interest payable after August 31st, 1922) ;
- (f) Interest on 4% and 5% Prize Loans issued in 1921, 1922 and 1923 by the *Fédération des Coopératives pour Dommages de Guerre* ;
- (g) Coupons and redemption premium on the 6% Bonds issued in 1924 by the *Association Nationale des Industriels et Commerçants* (Article 3 of Law of May 26th, 1924).

² No tax is due if income from deposits is less than 25, 50 or 100 francs for three months, six months or one year respectively.

³ The reduced rate only applies when the interest allowed to each depositor does not exceed 200, 400 or 800 francs for three months, six months or one year respectively. Beyond these limits, deposit income is taxed at 15 per cent.

⁴ Article 3 of the Law of July 23rd, 1932 (*Moniteur* of July 31st, 1932). The procedure to be followed in order to obtain this reduction of tax is laid down in a Royal Decree.

⁵ These conditions are :

- (a) The institutions must have their own administration ;
- (b) The directors must give their services free, except for the allowances in respect of their actual expenses or compensation for loss of a day's work through attendance at board meetings ;
- (c) The dividend paid to members on their share of paid-up capital must not exceed 5 per cent net.

⁶ Special rules are laid down for colonial companies in the Law of June 21st, 1927 ; see page 54.

⁷ The tax is not due on interest on the above-mentioned bonds issued free of Belgian tax since January 1st, 1926, unless the income accrues to persons or firms domiciled, resident or established in Belgium. In this case, the tax is 5 per cent and is payable either by the intermediary, who pays the income in Belgium, within a fortnight of payment, or by the actual recipient on the basis of an annual declaration, if he receives the coupon directly abroad.

⁸ Until the expiry of current contracts, this rate applies to the income from capital placed by the above-mentioned individuals and legal entities at the disposal of Belgian firms before July 16th, 1930.

C. *Income other than Annual Income.*

	Percentage rate of tax
16. Premiums or prizes of national public funds :	
Not exceeding 25,000 francs	3
Not exceeding 50,000 francs	4
Not exceeding 100,000 francs	6
Not exceeding 150,000 francs	8
Exceeding 150,000 francs	10

D. *Special Tax assimilated to Personal Property Tax, deducted at Source.*

17. Yield from lease of hunting and fishing rights ¹	10
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III. PROFESSIONAL TAX (TAX ON INCOME FROM TRADE AND PROFESSIONS).

Income ² (in francs)	Percentage applicable to the total amount of income ³	Amount of the tax corresponding to the income equal to the first figure of the "Income" column (in francs) ³
1. Not exceeding 50,000 ⁴		
2. Exceeding 50,000 :		
From :		
50,000 to 60,000	5.0	2,500
60,000 to 70,000	5.5	3,300
70,000 to 90,000	6.0	4,200
90,000 to 110,000	6.5	5,850
110,000 to 130,000	7.0	7,700
130,000 to 150,000	7.5	9,750
150,000 to 175,000	8.0	12,000
175,000 to 200,000	8.5	14,875
200,000 and upwards	9.0	

¹ This tax is payable by the tenants or, failing them, by the beneficiaries of the income, provided the latter amounts to 100 francs. It must be paid within a fortnight of the receipt of the income.

² For personal exemptions and deductions for dependents, see page 61.

³ In accordance with Article 7 of the Law of March 23rd, 1932, which fixes a special surcharge for 1932 and 1933, the figures below should be increased by 10 per cent (see page 61, note 2).

⁴ For income less than 50,000 francs, there exist various tariffs according to the population of the commune in which the taxpayer resides, which are too long to be reproduced here. The tax goes from 12 to 2,256 francs, according to the amount of the income and the number of dependents of the taxpayer (see also page 61).

IV. COMPLEMENTARY PERSONAL TAX.

Taxable basis ¹ (in francs)	Percentage applicable to the total amount of the taxable basis	Amount of tax corresponding to the income equal to the first figure of the " Taxable basis " column (in francs)
1. Not exceeding 15,000.	nil	nil
2. From 15,000 to 25,000	1	150
25,000 to 50,000	1.5	250
50,000 to 75,000	2	625
75,000 to 100,000	2.5	1,125
100,000 to 125,000	3	1,750
125,000 to 150,000	4	2,500
150,000 to 175,000	5	3,500
175,000 to 200,000	6	4,750
200,000 to 225,000	8	6,250
225,000 to 250,000	10	8,250
250,000 to 275,000	12	10,750
275,000 to 300,000	14	13,750
300,000 to 325,000	16	17,250
325,000 to 350,000	18	21,250
350,000 and over	20	25,750

¹ See, for the constitution of the taxable basis, deductions and exemptions, pages 64 to 66.

CZECHOSLOVAKIA

BY

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Minister Plenipotentiary,

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PART I. — GENERAL DESCRIPTION OF DIRECT TAX SYSTEM.¹

The system of direct taxation in Czechoslovakia is made up in the main of the following taxes :

Its basis is the income tax (*Einkommensteuer* or *Globalsteuer*),² which is levied upon the total income of every individual. This tax is supplemented by the following schedular taxes : the general tax on profits (*allgemeine Erwerbsteuer*) imposed on individuals and partnerships; the special tax on profits (*besondere Erwerbsteuer*), levied upon companies; the land tax (*Grundsteuer*); the buildings tax (*Gebäudessteuer*); the capital yield tax (*Rentensteuer*); the directors' percentages tax (*Tantiemensteuer*); and the tax on high salaries (*Besoldungsteuer*).³ Each of these taxes is levied upon income from a specific source — e.g., income from profit-making concerns, income from land, income from personal and other property, directors' percentages and from salaries in excess of a certain figure.

The provisions governing direct taxation in Czechoslovakia are embodied in the Law of June 15th, 1927 (No. 76 of the *Collected Laws and Decrees*), as amended by two laws, the more important of which is that of November 27th, 1930 (No. 167 of the *Collected Laws and Decrees*). Unless otherwise stated, the paragraphs quoted below refer to Law No. 76, of 1927.

I. INCOME TAX.

1 and 2. TAXPAYERS AND TAXABLE INCOME.

This tax is imposed exclusively upon individuals and estates in abeyance (*hereditas jacens*). It is assessed upon the net income of each household — i.e., on the total income in cash and in kind accruing, after deduction of expenses necessary to acquire and preserve that income and of legal abatements, to the head and members of a family. The wages and salaries of the latter, however, are not included in the reckoning.

Liability to pay this tax rests with the following persons, irrespective of nationality :

(1) Persons who are domiciled in the country or reside there for more than a year. — Whatever their nationality, *their tax-liability is unlimited* — that is, they are taxable in respect both of income derived from abroad and of income they acquire within the country. Under certain conditions, however, they are exempt from the tax in respect of the part of their income derived from real estate or enterprises situated abroad or from salaries or pensions paid by a foreign Government. In order that exemption may be granted, proof must be forthcoming that the part of the income in question has already paid income tax or a similar tax abroad; further, the foreign State must grant

¹ Legislation in force on April 30th, 1933.

² The German terms quoted in parentheses are the names of the Austrian taxes in which the Czechoslovak taxes have their origin.

³ Out of a total public revenue for 1930 of 7,377 million Czechoslovak crowns, revenue from direct taxes amounted to 1,752 millions. This sum was made up as follows: income tax, 1,161 millions; other direct taxes, 391 millions; local taxes and surtaxes, 200 millions.

reciprocal exemption, in virtue either of its domestic law or of treaties with Czechoslovakia (such as have already been concluded by Germany, Austria, Italy, Hungary and Poland).

An individual's domicile (*Wohnsitz*) is the place where he is living under conditions which imply an intention to reside there permanently (Section 252 of the law on direct taxation). In practice, a person who lives in Czechoslovakia for at least a year acquires a residence (*Aufenthalt*) in the country, which creates, in his respect, an unlimited fiscal obligation. The difference between domicile and residence is a matter of intention. An individual who comes to Czechoslovakia with the intention of remaining there permanently acquires a domicile in the country and becomes liable to tax forthwith. If he does not intend to remain in the country indefinitely, but does stay there for over a year, he becomes liable for that year and for the length of his stay.

(2) Persons who are not domiciled in the country and do not reside there for more than a year. — These persons have a *limited tax-liability*; they are taxable :

(a) If they are in receipt of :

(1) Income from real estate situated in Czechoslovakia, from loans secured by a mortgage on real estate situated in the country, and from property sequestrated or in some way legally immobilised in Czechoslovakia ;

(2) Income from profit-making enterprises or occupations carried on within the country or from participation in such enterprises or occupations ;

(3) Salaries or pensions paid by the State or by a province, district or commune :

(4) Czechoslovak directors' percentages.

(b) If they reside in the country for less than a year, for the purpose of doing business there. — In such case they are liable in respect of the income they receive during their period of residence within the country.

3. ASSESSMENT OF TAX.

(a) COMPUTATION OF TAXABLE INCOME.

The tax is assessed for each calendar year on income actually received during that year, even if the obligation to pay tax has arisen or has lapsed in the course of that year (paragraphs 23, 24). If the taxpayer's regular accounting period does not coincide with the calendar year, tax may, at the taxpayer's request, be computed on the results of the accounting period closed in the course of the taxable year, provided that this period covers a full twelve months.

The commercial profits of taxpayers whose accounts are kept in conformity with the Commercial Code¹ and customary usage are determined on the basis of those accounts, regard being had to the special provisions of the law on direct taxation (paragraph 10).

On the expiry of the fiscal period, and, in any case, not later than February of the following year, every taxpayer has to make a return of his income on a form prescribed by law. This return serves as the basis for determining the taxable income.

The return is checked with the taxpayer's participation. He may be required to furnish documentary confirmation of his statements and evidence by experts or other witnesses ; and the competent authority — *i.e.*, the tax commission — must take account of any proof the taxpayer may submit. If the taxpayer for no valid reason fails to make his return within the prescribed time or

¹ According to paragraph 28 of the Commercial Code, commercial books must be so kept as clearly to show the trader's operations and fortune. Entries in the books are governed by the accountancy regulations.

does not comply with the invitation to assist the authorities in checking his return, the tax is assessed on the basis of whatever material is at the authorities' disposal.

The taxpayer may be represented by a proxy (paragraph 263), who must be a Czechoslovak national enjoying full civil and political rights and who must produce his power of attorney. The latter must be in writing and must confer on the proxy the right to represent his principal in all matters pertaining to taxation.

Taxpayers living abroad must appoint a proxy who is domiciled in Czechoslovakia ; the same applies to any owner of an enterprise who is domiciled abroad and has no agent in the country. If taxpayers fail to conform to this rule, official notices, more particularly demand notes, are served on them as follows : the document is delivered to the authorities of the commune in which the taxpayer was last known to have been domiciled. These authorities make public announcement of delivery and, if the person concerned does not respond within four weeks of this announcement, the document is deemed to have been served (paragraph 257).

(b) COMPUTATION OF TAX.

The tax is computed as a fraction of the taxable income and increases progressively from 1 to about 29 per cent (see Annex).

Persons, however, whose incomes do not exceed a certain sum are exempt. This sum, in principle 7,000 Czechoslovak crowns, increases with the number of persons maintained by the taxpayer and may amount to as much as 11,000 crowns. But, as the tax-free minimum also includes income not liable to tax by reason of its origin (income, for example, received by a foreigner which is not liable to tax in Czechoslovakia), it is possible, though very rare, for tax to be levied on income below the above-mentioned sums.

Large families with incomes below 52,000 Czechoslovak crowns pay the tax at a reduced rate according to the size of the family (paragraph 20). On the other hand, bachelors, and married persons without children, whose incomes exceed 26,000 crowns, pay a surtax of 15 and 10 per cent respectively (paragraph 19).

Salaries and wages are taxed at a reduced rate. The tax on income other than salaries and wages is assessed by tax committees, each consisting of an official and of representatives of the taxpayers.

4. COLLECTION OF TAX.

Each taxpayer is informed of the amount of tax he owes through a demand note. He may appeal against his assessment by application to the higher administrative jurisdiction within thirty days of receiving the note. He may also, if necessary, appeal against the decision of this jurisdiction to the Supreme Administrative Court.

The tax is, in principle, payable by the taxpayer himself in four equal instalments on January 1st, April 1st, July 1st and October 1st of each year (paragraph 269). Until the taxpayer receives the demand note for the current year, he must make his quarterly payments on the basis of the note received the year before (paragraph 270), amounts thus paid being credited to the tax account for the current fiscal year.

The tax on salaries and wages is collected by deduction at the source and is paid to the Treasury by the employer.

II. GENERAL TAX ON PROFITS

1 and 2. TAXPAYERS AND TAXABLE INCOME.

This tax is imposed upon individuals and partnerships (as such) carrying on an occupation or engaged in trade or industry in Czechoslovakia (paragraph 46). By " persons " in this connection

the law understands, not only individuals, but also partnerships not liable to the special tax on profits. That is, ordinary partnerships (*öffentliche Handelsgesellschaften*), limited partnerships (*Kommanditgesellschaften*) and joint ventures (*Gelegenheitsgesellschaften*).

The tax is not imposed on salaries or wages, on profits from agricultural, horticultural and forestry operations, hunting and fishing conducted or engaged in by taxpayers on their own land, or on profits from enterprises liable to the special tax on profits. It is levied upon every enterprise forming an independent economic unit. The same applies when an enterprise has several establishments or operates in different places.

If an enterprise liable to this tax extends its operations to foreign countries from an establishment in Czechoslovakia (or, if it has no establishment proper, from the owner's domicile), tax will be assessed upon the total profits.

On the other hand, if such enterprise operates abroad permanently, and especially if it has a foreign branch, factory, purchase or sales office, agency or other establishment, it will be taxed on its foreign profits, only if these have not already been taxed abroad. At the same time, at least one-quarter of the enterprise's total profits will always be deemed to have been earned in Czechoslovakia.

Foreign enterprises which similarly extend their operations to Czechoslovakia are liable to the general tax on profits, only in respect of that part of their business which is situated in the country (paragraphs 48 and 49).

3. ASSESSMENT OF TAX.

(a) COMPUTATION OF TAXABLE INCOME AND ABATEMENTS.

The sum taxable is the net profit of the enterprise.

The taxable income of partnerships includes the share of profits accruing to each partner.

The taxable net income, for purposes of this tax, is, in principle, determined in the same way as for purposes of income tax. It may, however, be well to indicate the items that may or may not be deducted from gross profits in order to obtain net profit.

i. The following deductions *are* allowed :

(a) All expenses necessary in order to earn and maintain profits — viz. :

Expenses of operation and administration, general overhead and interest on business debts ;

Normal depreciation to provide against deterioration and wear and tear of buildings, machinery, tools and all other plant or materials used in the business ;

Capital losses (in particular, falls in the rate of exchange, actual or anticipated) ;

Premiums paid for the insurance of assets invested in the enterprise ;

Rent and royalties paid for the use of building, land and patents used in the business ;

Direct taxes and their surtaxes including turnover and other taxes which are assessed by the means of assessment lists and contributions in lieu of surtaxes or local taxes (these contributions must, however, be directly connected with the conduct of the business and must actually have been paid to the competent authorities).

Since 1927, taxpayers who keep regular books are also allowed to deduct a reasonable sum representing a reserve put aside for payment of the general tax on profits. In order to benefit by this provision, the taxpayer must show that, during the following fiscal year he applied the sum so deducted to the payment of profits tax and surtaxes within the legally prescribed time-limit.

(b) In the case of taxpayers keeping regular accounts who build or rebuild premises for the conduct of their business or the accommodation of their staff, or who build annexes to these premises, and in the case of enterprises which renew their machinery and tools : 20 per cent of the actual cost of this building or of these tools or machines. This deduction may be

made during the five years following the year in which the buildings were completed or the tools and machinery replaced; apart, too, from the deductions which these enterprises are already entitled to make for depreciation. If within ten years of their completion such buildings are put to some other use than that originally intended, the taxpayer must pay tax on the sums which he had originally been allowed to deduct from his taxable income under the heading of these new buildings.

(c) Enterprises which derive income from the possession or exploitation of real property are allowed to deduct from their profits liable to general tax on profits a sum corresponding to the amount on which land tax or buildings tax was levied.

(d) Enterprises which keep regular books and can show that for the two preceding business years they have uninterruptedly held at least 20 per cent of the shares, mining shares, bonus shares, etc., of another national enterprise liable to the special profits tax need not include the income from these securities among profits liable to tax if they bought them out of their own funds. If these securities were not acquired altogether out of the enterprise's own funds, only so much of the income therefrom may be deducted from taxable profits as exceeds the sum necessary to pay the interest on capital borrowed for the purpose.

2. The following deductions from taxable income are *not* allowed :

(a) Income tax, war tax, war-profits tax, property tax and general tax on profits, due in respect of years prior to 1927 ;

(b) Interest on the taxpayer's private debts, his personal obligations and life insurance premiums on behalf of the taxpayer himself or members of his family ;

(c) Taxes due — *i.e.*, taxes not yet paid, subject to what has been said above ;

(d) Repayment of debt or expenses incurred in enlarging or developing the enterprise, unless it is to be held that these sums are normally covered by the enterprise's profits ;

(e) Losses and depreciation of the taxpayer's capital and property, so far as such losses and depreciation are not directly connected with business operations, and losses from the acquisition of property at a price in excess of its real value ;

(f) Interest on capital invested by the taxpayer personally in his own enterprise ;

(g) Cost of the housing and maintenance of the taxpayer, his family and his servants, including the cash value of products consumed in kind ;

(h) Gifts and subsidies freely made, except such as the conduct of the business necessitates ; (Payments by the taxpayer for the purpose of insuring his staff against sickness or accident, retiring pensions and pensions for widows and orphans of employees may only be deducted up to the amount which the employer is legally bound to pay. An enterprise may not deduct from its profits the taxes it pays on behalf of its staff, even if under contract to pay them.)

(i) The tax on capital yield withheld by the debtor enterprise and paid on its creditor's behalf.

(b) COMPUTATION OF TAX.

The normal rate of tax is 2.5 per cent of the taxable profit. This, however, is reduced to 0.5 per cent in respect of profits not exceeding 30,000 Czechoslovak crowns and is increased to 4 per cent in respect of profits in excess of 140,000 crowns. Various advantages are further granted in respect of profits of less than 15,000 crowns.

In the case of enterprises whose capital exceeds 100,000 Czechoslovak crowns, the tax may not be less than 0.5 per thousand of the capital engaged in the business.

The tax on profits is subject to a surtax on behalf of the local authorities.

4. COLLECTION OF TAX.

The collection of the general tax on profits, like its assessment, is governed by the same rules as apply to income tax. A different method of collection is only adopted in respect of hawkers, itinerant vendors, etc. In their case, the tax is paid in advance and once for all. Partners who are personally responsible for the debts of their partnership are regarded as joint sureties for payment of the general tax on profits for which the partnership is liable. Similarly, a lessor is responsible for the profits tax owing by his tenant or lessee.

III. SPECIAL TAX ON PROFITS.

1 and 2. TAXPAYERS AND TAXABLE INCOME.

The special tax on profits is levied upon what are regarded by fiscal legislation as legal entities — viz. :

(1) Enterprises which are required by law to publish a balance-sheet — e.g., share companies (*Aktiengesellschaften*), limited partnerships with share capital (*Kommanditgesellschaften auf Aktien*), mining companies (*Berggewerkschaften*), insurance companies, savings banks (*Sparkassen*) and people's banks (*Vorschusskassen*), agricultural credit institutions (*Landeskreditinstitute*), together with State enterprises and public corporations ;

(2) Limited liability companies (*Gesellschaften mit beschränkter Haftung*) ;

(3) The brewers' corporations (*Brauberechtigte Bürgerschaften*).¹

(4) Profit-making enterprises of which at least half the capital is held by a foreign company (corporation, limited partnership with share capital, mining company or limited liability company) having no permanent establishment in Czechoslovakia and therefore not being itself taxable in Czechoslovakia.

If a Czechoslovak enterprise liable to the special tax on profits extends its activities from its establishment within the country to a foreign country where it has no permanent establishment, it is taxable in respect of all profits from these extended activities. If, however, the enterprise has some permanent establishment abroad, such as a branch, factory, purchase and sales office, agency or other means of conducting business, the foreign profits will be taxed in Czechoslovakia, only if they have not already paid abroad a schedular income tax levied by a foreign State. In these circumstances, the proportion of profits not taxable in Czechoslovakia may not exceed a certain maximum fixed as follows :

(a) In the case of enterprises which buy in Czechoslovakia and sell abroad or *vice versa*, the maximum exempt from taxation is half the profits of the foreign operations.

(b) If the enterprise manufactures in Czechoslovakia and sells abroad, only one-third of such profits may be deducted from the amount taxable in Czechoslovakia.

Similar provisions apply to foreign enterprises which extend their operations to Czechoslovakia or have an establishment in the country.

(c) In cases other than those covered by (a) and (b), the minimum taxable in Czechoslovakia is one-tenth of the total profits of Czechoslovak enterprises which do business abroad.

¹ The brewers' corporations are very ancient corporations which enjoy the right to brew beer in certain urban buildings.

The above rules are subject to a number of exceptions applying to operations in countries with which Czechoslovakia has concluded double-taxation conventions. Such countries are Austria, Hungary, Germany, Poland and Italy.

3. ASSESSMENT OF TAX.

The special tax on profits is fixed annually on the basis of a declaration which taxpayers are required to make within a fortnight of the passing of the accounts by the general meeting of shareholders and within six months of the close of the taxable business period.

(a) COMPUTATION OF TAXABLE INCOME AND ABATEMENTS.

The taxable amount consists of the net profits as legally established for the business period ending in the course of the tax year. The taxable profit is computed on the basis of the profits shown in the balance-sheet, plus expenses and losses not legally deductible and minus items which the law allows to be deducted.

(1) The following are the items which have to be *added* to the profits as shown in the balance-sheet.

(a) Profits of the taxable period devoted to increasing the enterprise's capital ;

(b) Profits of the taxable period devoted to repayment of capital invested in the enterprise by partners or members or to such extinction of debt as will increase the assets of the enterprise, or to the repayment of advances or subsidies not liable to the special tax on profits (see below, point (2) (c)) ;

(c) Profits devoted to paying interest on capital invested in the enterprise by partners and other shareholders, whether such capital is in the form of shares, beneficiary shares or in some other form of participation ; interest on loans proper, however, is deductible ;

(d) Profits devoted to subsidies, guarantees or advances to other enterprises ;

(e) Subsidies, gifts, etc., unless these are necessary to the conduct of the business ;

(Accordingly, contributions to sickness, disablement, old-age, accident and pensions insurance funds paid by the enterprise on behalf of its employees or of the latter's widows and orphans, over and above what it has to contribute by law, are not deductible ; nor are any taxes which the enterprise may pay on behalf of its staff, even if these payments are compulsory under a contract.)

(f) Profits devoted to the payment of the special tax on profits and its surtaxes ; (These taxes, however, may be deducted for fiscal periods subsequent to 1928, if it can be shown that the enterprise paid them during the tax year. Similarly, reserves set aside for payment of special tax on profits may be deducted if they are proportionate to the amount of tax due and if the enterprise can show that it actually paid the taxes in question in the course of the following tax period and within the prescribed time-limit.)

(g) Receipts set aside for payment of the tax on capital yield and withheld at the time of paying the taxable income to the beneficiaries thereof ;

(h) Profits of the current financial period devoted to making good losses brought forward from previous years.

(2) The following items must be *deducted* from the profits figuring in the balance-sheet :

(a) Profits brought forward from previous years ;

(b) Profits from property subject to land or buildings tax, up to the amount subject to the one or the other of these taxes ;

(c) Advances and grants made to the enterprise by the State and subsidies and other sums received by the enterprise ;

(d) In the case of insurance companies, the technical reserves corresponding to current risks and to compensation due, but not yet paid, in respect of losses already sustained ;

(e) Interest on loans (but see above, point (1) (c)) ;

(f) Funds necessary to provide against depreciation and wear and tear of movable property and material used in the business and sums representing loss of assets due to fluctuations in the exchange or other factors. Profits placed to special reserve for depreciation and losses may also be deducted, but only if the nature of the losses and depreciation thus provided against is specified and if the said depreciation and losses have already been incurred or are to be regarded as probable. Deduction may also be made of profits on the rate of exchange, which, if not actually realised, appear in the accounts and which savings banks and insurance companies would assign to special reserves to cover losses on the rate of exchange.

(g) In the case of enterprises keeping regular accounts which build or rebuild premises for the conduct of business or the accommodation of staff or which build annexes to these premises and, in the case of enterprises which renew their machinery and equipment annually, 20 per cent of the actual cost of this building or of this machinery and equipment may be deducted during the five years following the year in which the buildings were completed or the equipment and machinery replaced ; apart, too, from the deductions which these enterprises are already entitled to make for depreciation. This provision has been in force since 1928. If within ten years of their completion such buildings are put to some other use than that originally intended, the taxpayer must pay tax on the sums which he had originally been allowed to deduct from his taxable income under the heading of these new buildings.

(h) Remuneration paid to employees for their services, such remuneration being regarded as expenses necessary to the conduct of the enterprise.

Gifts for the purpose of adding to the compensation payable to employees in the event of old age, disablement or retirement, and pensions to their widows and orphans, are deductible if these sums are paid to the employees or their families direct or to pensions and benefit funds having a legal existence apart from that of the enterprise. The fiscal authorities may, further, in deserving cases, allow the deduction of grants made on behalf of employees to pensions or benefit funds not legally distinct from the enterprise, if such grants are normal and if the enterprise declares itself willing to pay supplementary tax, should the funds in question not be devoted to their original purpose.

(i) Shares of profits paid to employees, when due to them under their contract ;

(j) Remuneration paid by savings banks to the members of their board of management or supervision.

In the case of other enterprises, remunerations to members of boards of management, supervisory committees, etc., may only be deducted on the following conditions : the members concerned must have legal right to this remuneration, and the services they render the enterprise must constitute their main occupation and be such as would otherwise have to be performed by a salaried employee ; further, such remuneration must not be dependent upon net profits, but be in proportion to the services rendered. Lastly, such remuneration may not exceed 30 per cent of net profits in the case of limited liability companies or 10 per cent in the case of other enterprises.

(k) In the case of enterprises which can show that they have for the two business years

preceding the taxable year uninterruptedly held at least 20 per cent of the shares, beneficiary and other, of a Czechoslovak company liable to the special tax on profits and that they acquired them out of their own funds, the dividends and other income from these securities are deductible. If the enterprise has not acquired these securities exclusively out of its own funds, only the amount in excess of the interest on capital borrowed for the purpose is deductible from the profits figuring in the balance-sheet.

(l) Although, in principle, the profits distributed to their members by manufacturing and agricultural co-operatives (*Erwerbs- und Wirtschaftsgenossenschaften*) are taxable, such associations are permitted to deduct an amount corresponding to remuneration paid for services rendered or material supplied by their members. This provision also applies to such similar associations as sugar-producers associations which are incorporated as companies by shares.

(m) Annuities paid by the State for enterprises it has repurchased or taken over may be deducted from taxable profits on condition that these enterprises were already exempt from the special tax on profits under provisions in force before the enactment of the law on direct taxation.

When the legally deductible expenses concern enterprises or profits which are only partially liable to the tax (as in the case of firms doing business both in Czechoslovakia and abroad), deduction is confined to the fraction of expenses corresponding to the amount of profits taxable, and, if it is impossible to establish an exact relation between these expenses and profits, deductible expenses are apportioned on the basis of gross receipts.

(b) COMPUTATION OF TAX.

The normal rate of the tax is 9 per cent. Co-operative societies which only trade with their members (*Selbsthilfsgesellschaften*) pay tax at 2 per cent of their capital. The rate is increased from 2 to 5 per cent according to the amount of profit taxable, when manufacturing or agricultural co-operatives (*Erwerbs- und Wirtschaftsgenossenschaften*) are allowed under their statutes to trade with persons who are not members of the co-operative. The tax rate varies from 1 to 4 per cent for saving banks, welfare institutions, educational establishments, etc. The tax is subject to surtaxes on behalf of various public corporations. Further, when taxable profits exceed 6 per cent of the paid-up capital, the tax is supplemented by an "excess-profits tax" called the *Rentabilitätszuschlag*. The rate of this surtax is from 2 to 6 per cent of taxable profits in the case of share companies, limited partnerships with share capital, mining companies and limited liability companies, and from 2 to 4 per cent in the case of co-operatives trading with third parties. The surplus assets of taxable enterprises in course of liquidation are subject to the special profits tax inasmuch as they do not comprise amounts which have not already been taxed, but the excess-profits surtax is replaced by a liquidation surtax fixed at 4 per cent of taxable profits.

The excess-profits and liquidation surtaxes are not subject to supplementary taxes on behalf of public corporations. The special tax on profits may not fall below 1 per thousand of the capital invested in the enterprise. In the case of insurance companies incorporated in the form of share companies, the tax may not be less than 1 per thousand of the total net premiums received during the tax year.

4. COLLECTION OF TAX.

The provisions governing the payment and assessment of the special tax on profits are the same as those governing income tax. The assessment, however, is made, not by a tax commission, but by the fiscal administration itself.

IV. LAND TAX.

The land tax is imposed upon all income from arable land and agricultural estates in Czechoslovakia, irrespective of the domicile or residence of the beneficiary of such income. Land situated abroad is not subject to this tax, even if it belongs to persons domiciled or resident in Czechoslovakia.

Certain forms of land, especially unproductive land, land built on together with its appurtenances, roads, railways and their annexes, are automatically exempt from the tax.

At the owner's request, the law also allows the exemption of certain real property, such as nursery gardens and vineyards, dykes, canals and reservoirs. Temporary exemption may also be granted to land newly taken into cultivation, recently planted or grafted vines and, finally, land on which agricultural settlements have been newly established.

The tax is payable by the registered owner of the land.

The taxable income is obtained by multiplying by 20 in the case of forests, and by 17 in the case of other land, the value of the property as recorded in the land register. (The original register dates from 1869 and has been only summarily revised.) Since the tax is assessed on cadastral income, no return need be made, and the authorities do not normally deliver individual demand notes. Taxpayers are informed of the tax due from them by public notice issued in the commune where the taxable property is situated. As a rule, they only receive a personal demand note, if, as the result of changes in the register, the amount of tax is different from that of the previous year. A demand note will, however, be sent to any taxpayer at his express request. The tax, which is fixed at 2 per cent of the taxable total, is increased by an additional tax of 1½ per cent collected at the same time as the principal tax, and by various surtaxes levied on behalf of the provinces, districts, communes and other public corporations.

V. BUILDINGS TAX.

The buildings tax, like the land tax, is purely territorial and is levied exclusively on income from buildings situated in Czechoslovakia. The persons liable to buildings tax are the owners or usufructuaries of the taxable property.

The tax is imposed, not only on the income from buildings permanently attached to the soil, but on the soil itself upon which these buildings and annexes thereof (courtyards, etc.), stand. Exemption is granted to Government buildings occupied by a public service, buildings exempted under special conventions concluded by the State, buildings belonging to foreign States and in use by their diplomatic and consular representatives (subject to reciprocity), churches, barracks, buildings for the use of social insurance institutions, industrial buildings, etc. Further, certain buildings, and particularly those which are devoted free of charge to some public purpose, may be exempted at the owner's request. Lastly, temporary exemption is granted to new buildings.

The tax is divided into two categories :

(a) *The rent tax (Zinssteuer)*, imposed in certain specified localities enumerated in the law, on all buildings whether let or not, and in other places only on buildings actually let ; this tax is computed on the gross rental or, as the case may be, the rental value ; the rate is 12 per cent in Prague, Brno and Bratislava and 8 per cent elsewhere ;

(b) *The graduated tax (Klassensteuer)* is imposed on unlet dwelling-houses situated outside places compulsorily liable to the rent tax. It is computed on a sliding scale according to the number of rooms in each house.

The graduated tax is assessed on the basis of the entries in the land register, while the rent tax is determined according to the returns which the taxpayers in question are required to furnish to the authorities. Both categories of buildings tax are subject to provincial and local surtaxes.

Annual demand notes are sent in respect of the rent tax only. In the case of the graduated tax, taxpayers are informed of the amount due by a notice published by the competent communal authority.

VI. TAX ON CAPITAL YIELD.

The tax on capital yield is levied on income from personal and real property which is not taxable under the heading of land tax, buildings tax or general or special tax on profits. Individuals who are domiciled in Czechoslovakia or who have resided there for more than a year and corporations having their head office in the country are liable to this tax in respect of any income, of whatever origin, which by its nature comes within the purview of this tax. Other individuals and legal entities are only liable in respect of income of this kind when they derive it from, or receive it in, Czechoslovakia.

In particular, the following income is liable to this tax : interest on loans contracted by the State or public corporations or by private companies, partnerships and individuals domiciled in Czechoslovakia ; interest on deposits with savings banks and credit institutions, current accounts, sureties and other credits ; interest and commissions on discount operations ; income from the lease of a business ; annuities (with certain exceptions) ; maintenance allowances ; annual royalties from the concession of patents or other similar property ; interest and dividends from foreign bonds and securities.

These last, however, are not subject to tax on capital yield if it can be shown that they are subject abroad to a special direct tax other than income tax. Further, shares in foreign enterprises which have an establishment in Czechoslovakia and which are there subject to the special tax on profits are not regarded as foreign securities and are therefore not liable to tax on capital yield.

The rate of the tax is 3 per cent if paid direct, and 6 per cent if deducted at the source. In some cases, however, the rates differ, the scale ranging from 1 to 10 per cent. If the tax is paid by the taxpayer himself, it is subject to a surtax in favour of the provinces, districts, communes, etc., but, if it is collected at the source, no surtax is imposed.

The tax is collected at the source in the case of payments made by the State, provinces or other public institutions ; by districts or communes or by enterprises liable to the special tax on profits ; if these payments are interest or other income from bonds or securities issued by these institutions and enterprises (whatever may be the manner in which payment is made or shown) or interest on deposits with savings banks ; when individuals or corporations professionally engaged in banking pay their customers, or credit their customers' accounts with, interest of almost any kind. The only interest excepted is interest on exchange or discount operations and interest credited to another person also professionally engaged in banking.

As a general rule, institutions or enterprises which withhold the tax at the time of paying the taxable income pay the sums thus withheld twice a year to the Treasury accompanied by a list of the sums, but not mentioning the names of those to whom the payments were made.

In all cases not enumerated above, the tax is paid direct by the beneficiaries of the taxable income on the basis of a return. If the taxable income consists wholly or in part of products of the soil or of nature, these products are assessed at their market value. Further, it is not usual to deduct from taxable income the interest on debts attaching to that income.

VII. DIRECTORS' PERCENTAGES TAX.

The remuneration paid to directors of share companies or limited partnerships with share capital is liable to directors' percentages tax. The tax is at the rate of 10 per cent and is not subject to any surtax on behalf of public corporations. It is deducted by the companies in question at the time of paying the taxable income and is paid by them to the Treasury. When the total of

such remuneration paid by a company does not exceed 5,000 Czechoslovak crowns a year, it is tax-free. Salaries and emoluments payable by companies to their directors under service contracts are not liable to directors' percentages tax, but pay the tax on high salaries.

In the case of remuneration paid to persons domiciled abroad, the tax has also to be deducted at the time of paying the remuneration. Thus, Czechoslovak branches of foreign share-companies or limited partnerships with share capital have to withhold and pay the tax, not only when they themselves distribute the taxable remuneration, but if they transmit these payments to the foreign enterprise to which they belong.

In order, however, to avoid double taxation, certain exceptions to this principle have been provided for by international agreement. Thus, Austria and Hungary have arranged that the tax on directors' percentages shall be collected exclusively by the country in which is situated the head office of the debtor enterprise.

VIII. TAX ON HIGH SALARIES.

Salaries and emoluments liable to income tax are further subject to the tax on high salaries if, after deduction of expenses which are directly and economically related to the income, they exceed an annual sum of 100,000 Czechoslovak crowns. This tax, which is at the rate of 3 per cent, is subject to the surtaxes in favour of public corporations.

PART II. — TAXATION OF FOREIGN AND NATIONAL ENTERPRISES.

A. FOREIGN ENTERPRISES.

1. DEFINITION AND GENERAL PRINCIPLES.

Czechoslovak legislation does not expressly define the term "foreign enterprise", but, according to the Law of December 11th, 1919 (No. 12 of *Collected Laws and Decrees 1920*), an enterprise is national if it has its head office and centre of management in Czechoslovakia; otherwise, it is foreign.

A foreign enterprise is taxable in Czechoslovakia if it engages or participates in profit-seeking business in that country; and tax is levied only on profits from such business or interests. Accordingly, a foreign enterprise which has a branch, factory, purchase or sales office or agency within the country or does business there in some other form is, in principle, liable to tax on its profits from these establishments or operations. These profits will be subject to the general or special tax on profits according as the enterprise to which they accrue is liable by its nature to the one or the other of these taxes (see references to the matter in Part I).

The income tax is imposed upon all income earned in Czechoslovakia by an enterprise belonging to a single person and, in the case of enterprises belonging to a partnership, upon the proportion of income accruing to each partner. In the case of joint-stock companies or limited partnerships with share capital, income tax is levied on the shareholders' dividends, only if they are domiciled in the country or have lived there for a year.

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) DIVIDENDS.

Dividends of Foreign Origin.—Foreign enterprises in receipt of dividends which do not originate in Czechoslovakia are taxable thereon in the following cases:

(1) When these foreign dividends are part of the receipts of an establishment possessed by the foreign enterprise in Czechoslovakia. In such case, the dividend is regarded as part of the total profits of the Czechoslovak establishment and is liable to the general or to the special tax on profits according to the kind of enterprise (see Part I), and, in certain circumstances, to income tax, as explained above under "Definition and General Principles".

As an example, we may take the case of a bank whose head office is in Paris, but whose Czechoslovak branch has in its portfolio shares in a Roumanian company; the dividends paid on these shares will be regarded as part of the taxable profits of the establishment in Czechoslovakia.

(2) If the foreign dividends do not figure among the profits of the Czechoslovak establishment, they will be liable to the tax on capital yield, unless they can be shown to have paid abroad a special direct tax other than income tax.

(3) Capital yield tax will also be levied on these dividends if the foreign enterprise, though having no establishment in Czechoslovakia, nevertheless receives these dividends in that country through a bank established there.

Dividends of Czechoslovak Origin. — Dividends paid by Czechoslovak companies are, in principle, subject to the general or special tax on profits if they are part of the profits of the foreign enterprise's branch or establishment in Czechoslovakia. By way of exception, however, enterprises which keep regular accounts and prove that they have for the two business years which precede the taxable business year uninterruptedly held at least 20 per cent of the shares, beneficiary shares, and others, of a Czechoslovak enterprise liable to the special tax on profits, and that they acquired these shares out of their own funds, may deduct the profits corresponding to such dividends from their income liable to the general or special tax on profits. If, however, the securities in question were not acquired out of the enterprise's own funds, only the amount which exceeds the interest on capital borrowed for purposes of such acquisition may be deducted from the income liable to the one or the other of these taxes.

If dividends of Czechoslovak origin do not belong to the trading profits of the branch in Czechoslovakia, they are not liable to tax, having already been taxed as profits of the debtor enterprise.

The double-taxation conventions concluded by Czechoslovakia with Austria and Hungary expressly exclude shares from the provisions governing profit-making enterprises, with the result that dividends are never taxed as part of commercial profits, and a similar clause is contained in the convention with Italy. On the other hand, the conventions concluded with Germany and Poland have no such clause; the latter, incidentally, does not deal with the treatment of legal entities for purposes of direct taxation.

(b) INTEREST.

Interest on debts secured on real estate situated in Czechoslovakia is in all cases taxable in the country.

If such interest figures among the profits of the branch or establishment of a foreign enterprise in Czechoslovakia, it will be subject to the general or special tax on profits, according to the kind of enterprise. If it is not part of the profits of a Czechoslovak branch or establishment, it will be subject to the tax on capital yield (collected on the basis of the taxpayer's return) and in most cases to income tax.

The double-taxation conventions provide for no exceptions to this principle. In the case, however, of income tax, the convention with Germany stipulates that income from mortgage debts shall be taxed in the country where the creditor is domiciled.

Interest received by a foreign enterprise in Czechoslovakia on bonds and debts not secured on real estate will be liable to the tax on capital yield, unless it appears among the profits of a Czechoslovak branch or establishment of the foreign enterprise in question. In the latter case it will, along with the branch's other profits, be liable to either the general or the special tax on profits, according to the kind of enterprise.

Most of the double-taxation conventions provide that, when the State in which the interest has its origin deducts tax at the source, no tax may be levied by the other State. The convention with Poland alone allows the other State also to collect the tax. The convention with Italy lays down that the right to tax securities issued by the State, provinces, communes, other corporations, share companies, banks and credit institutions is vested in the State in which the creditor is domiciled.

(c) DIRECTORS' PERCENTAGES.

The taxation of directors' percentages paid in Czechoslovakia (such as the percentages distributed out of the profits of the Czechoslovak branch of a foreign enterprise) was dealt with in detail in Part I under the heading "Directors' Percentages Tax". These percentages, however, if accruing to individuals, are also liable to income tax, even when they are paid abroad.

Further, the double-taxation conventions confer the right to tax directors' percentages on the State in which the beneficiary is domiciled. An exception is the convention with Poland, according to which directors' percentages are liable to all the taxes of the country in which they are paid.

(d) ROYALTIES FOR USE OF PATENTS, COPYRIGHTS, TRADE-MARKS, SECRET PROCESSES AND FORMULÆ AND SIMILAR INCOME.

Authors and inventors and their heirs, legatees, assigns, etc., who themselves exploit their patents and copyrights are liable, if they have an establishment in Czechoslovakia, either to the general tax on profits and to income tax or to the special tax on profits. If there is no branch or establishment in the country, this income will be liable to the tax on capital yield, payable directly by the recipient of the income.

If the foreign holder of a patent or copyright, etc., grants the use of his rights in return for a periodical royalty, these payments will be subject to the tax on capital yield. If the remuneration takes the form of a single payment, it will be exempt from taxation.

(e) RENTS FROM REAL ESTATE, MINING ROYALTIES AND SIMILAR INCOME.

Income from real estate — *i.e.*, rents, mining royalties, annuities and other similar income from property situated in the country — is in all cases taxable in Czechoslovakia. Income from buildings is liable to the buildings tax and income from agricultural land to the land tax (see Part I). If the beneficiary of such income is an individual, he is also liable to income tax. Income from the lease of a business and other similar income not liable to either land tax or buildings tax is subject to the tax on capital yield.

If an enterprise liable to the special or to the general tax on profits leases a factory, mine or other property belonging to it, the income therefrom is liable to the one or the other of these taxes, after deduction of income already subject to land tax or buildings tax.

Profits from the exploitation of mines are liable either to the special tax on profits or to the general tax on profits and to income tax. The taxation of income from real estate situated abroad is treated under the heading (e) of page III.

All the double-taxation conventions lay down the principle that income from real estate is taxable only in the country in which the estate is situated.

(f) GAIN DERIVED FROM THE PURCHASE AND SALE OF REAL ESTATE, SECURITIES AND PERSONAL PROPERTY.

The profits which a foreign enterprise derives either within Czechoslovakia or abroad from the purchase and sale of real estate, securities and personal property are only taxable if the sale was in the course of the business which the foreign enterprise conducts in the country — that is, if it was effected by a branch or establishment situated in Czechoslovakia. Should such gains be taxable, they will be liable to the general tax on profits and income tax or to the special tax on profits (according to the nature of the enterprise).

(g) SALARIES, WAGES, COMMISSIONS AND OTHER REMUNERATION FOR SERVICES.

A person domiciled abroad who receives a salary or wage for services rendered in Czechoslovakia, for less than a year is not liable to tax. On the other hand, a person domiciled within the country or residing there for longer than a year is liable to income tax, and possibly to the tax on high salaries, in respect of all remuneration paid to him either within the country or abroad. The only exemption is in respect of salaries paid by foreign Governments. This exemption, however, is subject to reciprocity and is only granted if the salaries paid by the foreign country are taxable abroad.

All the double-taxation conventions concluded by Czechoslovakia lay down that salaries and other remuneration paid out of public funds shall be taxed by the country which makes these payments.

(h) INCOME FROM A TRUST.

The taxation of "trusts", as this term is understood by Anglo-Saxon law, is a question that does not arise in Czechoslovakia.

(i) INCOME FROM CARRYING ON A BUSINESS OR INDUSTRY.

Through :

(1) *A Local Commission Agent or Broker.* — The profits which an enterprise derives from operations conducted through a local commission agent or broker are not taxable.

(2) *A Local Dealer or Distributor.* — The same applies to profits from sales made to local dealers or distributors, even if the latter have an exclusive right to resell the goods.

(3) *A Travelling Salesman, whether or not having Power to conclude a Contract.* — Income from sales through a travelling salesman is not as a rule taxable.

(4) and (5). *A Local Agent with Power of Attorney or selling out of a Stock belonging to the Foreign Enterprise.* — If, on the other hand, the enterprise has an authorised proxy or agent, who sells out of a stock belonging to the enterprise and is, in fact, a permanent representative of the foreign enterprise, the latter must be regarded as having an establishment in the country.

It should be added that foreign enterprises having agents or employees carrying on permanently their activities in the country are deemed, within the meaning of the law, to possess a permanent establishment in the country

(6) *A Permanent Establishment of Any Kind.* — The income which a foreign enterprise derives from operations of a permanent establishment within the country is taxable and, according to the taxpayer's status, will be liable to income tax and the general tax on profits, or to the special tax on profits.

The double-taxation conventions are in accordance with the above principles and, except for the convention concluded with Italy, contain detailed provisions concerning what is meant by an establishment.

B. NATIONAL ENTERPRISES.

I. DEFINITION AND GENERAL PRINCIPLES.

According to the Law of December 11th, 1919 (No. 12 of *Collected Laws and Decrees 1920*), any enterprise is regarded as national which has its head office and centre of management in Czechoslovakia.

These enterprises are taxable in Czechoslovakia both in respect of profits they derive from operations in foreign countries where they have no establishment and in respect of profits from

operations conducted within Czechoslovakia. The profits of a foreign establishment are not subject to direct taxation in Czechoslovakia if they are liable to a similar tax abroad. However, a certain fraction of the enterprise's total profits is always deemed to have been earned within the country. This fraction is one-quarter for purposes of general tax on profits and one-tenth for purposes of special profits tax. The fact that an enterprise belongs to an individual, a partnership or a company is only of importance in determining the category of tax payable (see Part I with reference to the special tax on profits).

The various exceptions to these principles resulting from double-taxation agreements are mentioned under the next heading and Part III.

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) DIVIDENDS.

Dividends from foreign securities are, in principle, liable to the tax on capital yield (see above, page 106), unless it can be shown that they have already paid a special direct tax abroad.

If, however, these dividends are included among the profits of an enterprise situated in Czechoslovakia, they will be subject, like the whole of the enterprise's profits, to either the general or the special tax on profits. This does not apply to dividends forming part of the profits of an establishment situated abroad, since these profits, as already mentioned, are not taxable in Czechoslovakia.

Further, dividends accruing to an individual domiciled in the country or resident there for more than a year will also be liable to income tax.

The references to dividends in the double-taxation conventions were dealt with on page 107.

(b) INTEREST.

Interest on debts secured on real estate situated abroad is not as a rule exempt from taxation in Czechoslovakia.

If it forms part of the profits of a foreign establishment of a Czechoslovak enterprise, it is treated in the same way as the other profits of that establishment (see "Definition and General Principles" above).

Otherwise, it is subject to the tax on capital yield, provided it has not already paid a special direct tax abroad.

The conventions, except that concluded with Germany, confer the right to tax this interest on the country in which the real estate serving as security for the debt is situated.

Interest on unsecured debts and personal securities is normally taxed according to the same rules as dividends.

The exceptions provided in the conventions were mentioned under the corresponding heading referring to "Foreign Enterprises" (see page 107).

(c) DIRECTORS' PERCENTAGES.

Percentages distributed by foreign companies to persons domiciled in Czechoslovakia or resident there for more than a year are subject to income tax. The convention with Poland, as already explained (page 108), provides an exception to this rule. These percentages are also liable to directors' percentages tax in the circumstances explained in the chapter of Part I dealing with that tax.

(d) ROYALTIES FOR USE OF PATENTS, COPYRIGHTS, TRADE-MARKS, SECRET PROCESSES AND FORMULÆ AND SIMILAR INCOME.

(1) If an inventor or author domiciled in Czechoslovakia or resident there for longer than a year exploits his patent or copyright personally, he is liable to income tax. If this exploitation is more than an accessory occupation and brings him in enough to live on, he is further liable to the general tax on profits. This provision applies also to the heirs and assigns of authors and inventors.

(2) If the author or inventor in return for a periodic payment has sold his rights to some other person, who exploits the patent or copyright abroad, the author (or inventor) is liable to income tax and capital yield tax. If, however, the price received is not a periodic royalty but a single payment, it is not taxable.

(3) A person acquiring the right to exploit the patent or copyright will be liable to income tax, general tax on profits or special tax on profits.

(e) RENTS FROM REAL ESTATE, MINING ROYALTIES AND SIMILAR INCOME.

Income from real estate situated abroad (rents, mining royalties, etc.) is not taxable in Czechoslovakia if it has already paid income tax or some similar tax abroad. This condition, however, is subject to reciprocity. If the income is part of the profits from a foreign establishment of a Czechoslovak enterprise, it is governed by the rules explained under the heading "Definition and General Principles" on page 109.

Rents secured on real estate situated abroad and accruing to persons domiciled in Czechoslovakia are liable to the tax on capital yield (unless already subject to a special direct tax other than income tax abroad) and, if received by individuals, are also subject to income tax.

(f) GAIN DERIVED FROM THE PURCHASE AND SALE OF REAL ESTATE, SECURITIES AND PERSONAL PROPERTY.

Gain from the sale of personal or real property abroad is liable to income tax, if the sale was in the nature of a speculation.

While leaving it to the taxpayer to prove the contrary, the law assumes speculation if real estate is sold less than two years after it was bought, and if personal property (especially securities) is sold within three months of purchase.

If the transactions are ordinary business deals, as, for instance, in the case of real estate transactions, the profits are liable to income tax, the general tax on profits or the special profits tax, unless the operation was conducted by an establishment situated abroad.

(g) SALARIES, WAGES, COMMISSIONS AND OTHER REMUNERATION FOR SERVICES.

The salaries and wages paid abroad to taxpayers domiciled in Czechoslovakia are liable to income tax, and possibly to the tax on high salaries. Special provisions concerning salaries paid by foreign Governments were referred to above (see page 109).

(h) INCOME FROM A TRUST.

The taxation of "trusts", as this term is understood by Anglo-Saxon law, is a question that does not arise in Czechoslovakia.

(i) INCOME FROM CARRYING ON A BUSINESS OR INDUSTRY.

A national enterprise which does business abroad through a local commission agent or independent dealer is liable in respect of the profits from such business to the general tax on profits and income tax or to the special tax on profits, according to its status.

If the national enterprise does business abroad through persons attached to it by a contract and permanently established abroad, or through permanent representatives, the profits from these operations will be treated in the same way as those of an independent establishment situated abroad. If these profits are liable abroad to a tax similar to the general or special tax on profits, they will, in principle, be exempt from these taxes in Czechoslovakia. If it is further shown, that they are liable to income tax or a similar tax abroad, and if the foreign country grants reciprocal treatment, they will be exempt from income tax in Czechoslovakia.

PART III. — METHODS OF ALLOCATING TAXABLE INCOME.

A. FOREIGN ENTERPRISES WITH LOCAL BRANCHES OR SUBSIDIARIES.

I. GENERAL QUESTIONS AND METHODS OF APPORTIONMENT.

In the remarks that follow, consideration is mainly given to the solutions adopted by existing laws and regulations and in administrative practice. It should be added, however, that some of the conventions concluded with foreign countries, especially those with Austria, contain a number of exceptions to the normal rules of apportionment.

Article 3, paragraph 3, of the Austro-Czechoslovak Convention for the avoidance of double taxation in the matter of direct taxes (*Collected Laws and Decrees* of 1922, No. 414) provides that enterprises which have establishments in the two countries shall only be taxed in each in proportion to the extent of the operations carried on by the establishment situated in that country. The methods of apportionment must be fixed by agreement between the two Ministers of Finance. In conformity with this agreement, the Minister of Finance issued a Decree on January 29th, 1923 (No. 20, *Collected Laws and Decrees* of 1923), of which the following is an extract :

“ (1) In assessing taxation in respect of the sales office of a producing establishment—situated in the other State, the taxable business profits of the sales offices shall be reckoned as one-third of the total profits accruing to the establishment from the turnover effected through the sales office. Where the sales office also undertakes purchases, its share shall be reckoned as one-half. Where purchases are effected by a branch situated in the one State and sales by an establishment situated in the other State, the total profits accruing from such business transactions shall be divided equally. Profits accruing from joint operations of the two branches and which are to be apportioned between the two States shall be reckoned on the total profits of the undertaking in accordance with the ratio between the turnover resulting from such joint operations and the total business turnover of the undertaking. Where profits accrue exclusively from the operations of one of the two business establishments, they shall be reckoned on the total profits in accordance with the ratio existing between the turnover resulting from such operations and the total turnover of the undertaking. The fiscal authorities of the two States may jointly carry out the apportionment according to closed accounts, where it seems probable that such allocation will not differ appreciably from the estimated results of the application of the aforementioned principles of apportionment.

“ (2) In the calculations provided for in the foregoing paragraph, business turnovers expressed in different currencies shall be reckoned according to the average rate quoted on the Vienna Stock Exchange (average rate of payment on Prague) for the business period in respect of which taxes are payable. The average shall be calculated according to the rates on the 1st, 11th and 21st of each month of the period in question. In the event of no quotation being made on one of the specified days, the next quotation following this date shall be regarded as valid. Both parties agree that profits expressed in various currencies shall as a rule be converted at

the rate of exchange current on the day when the balance-sheet was drawn up ; where any other rate of conversion is adopted as a basis, the sanction of the two financial administrations shall in every case be required.

“ (3) Where an establishment in circumstances other than those already mentioned engages in business transactions on behalf of an establishment situated in the territory of the other State, the customary commission shall be regarded in the State in which these transactions are effected as the profits accruing from such transactions.

“ (4) If the results obtained by the application of the foregoing principles are in obvious contradiction with the actual situation in regard to profits, the two financial administrations may agree upon another method of apportionment ; in such case the taxpayer shall previously be heard by the financial administrations of either party.”

Another special agreement has been concluded with Austria concerning credit institutions and insurance companies. The profits of the former are allocated on the basis of the ratio between the staff expenses (*Personallasten*) of the establishment situated in the one country and those of the whole enterprise.

As between insurance companies, allocation is based on the ratio between the net annual premiums (after deducting bonuses) of the establishment situated in the one country and the total net premiums paid to the whole enterprise.

Further, the double-taxation convention concerning direct taxes concluded with Poland lays down that, when an enterprise has establishments in the territories of the two States, the joint receipts of these establishments shall as a rule be allocated according to the funds and capital employed by, or invested in, these establishments, and expenses in proportion to receipts. In some cases, the Ministers of Finance of the two States may agree upon another method of allocation. The receipts which one State earns from the sale of goods bought in another country, and the expenses corresponding to these receipts, shall, as a general rule, be apportioned equally between the establishments concerned in the operation.

(a) BOOK-KEEPING AND ACCOUNTING REQUIREMENTS.

The law on direct taxation does not prescribe the keeping of books and accounts by taxpayers, but it offers many advantages to those who do in fact keep regular accounts. The executive regulations for applying the law in question lay down that taxpayers who regularly keep the books prescribed by Articles 28 *et seq.* of the Commercial Code must base their profits on the results of the accounts and balance-sheet data for the taxable period.

Article 28 of the Commercial Code requires every trader and trading company to keep books in which are entered all their business operations and a statement of their property. Each operation must be entered separately. The law does not, however, prescribe the form of these entries. In practice, traders employ the usual methods of accountancy — that is to say, double-entry book-keeping, but large enterprises use the American or other methods. Commercial books must be kept in a living language. Traders are required to keep their books, letters received and copies of outgoing letters for ten years. They must draw up an inventory on opening business and, after that, annually. The inventory must contain an exact and classified statement of all the taxpayer's property and of his debts, owing both to him and by him. The balance-sheet must show the composition and nature of the taxpayer's assets and liabilities. Material used in the business must be entered at its utility value — *i.e.*, at the price which it would cost to replace it. Goods for sale must be entered at their sale price at the time of preparing the balance-sheet. Debts are recorded at their actual figure at the same time.

The provisions relating to the special tax on companies' profits (see Part I) are based on the presumption that these companies use double-entry book-keeping.

(b) METHODS OF ALLOCATION.

(1) *Method of Separate Accounting.*

The general tax on profits, the income tax and the special tax on profits, payable by foreign enterprises, are assessed exclusively on the results of the establishments situated in the country and the business they do in that country. The taxpayer or his representative is therefore required to submit a return accompanied by the balance-sheet and profit-and-loss account of the Czechoslovak establishment. The taxable profits, however, must not be less than the minima stipulated by the law (see No. (3) below). For purposes of computing these minima, no account is taken of operations of the foreign enterprise in which the Czechoslovak establishment takes no part.

The administration then checks the return and documents submitted in support thereof and compares them with any information at its disposal, such as statistics, particulars of similar enterprises, expert opinions, witnesses' testimonies, etc., and, if necessary, asks the taxpayer to furnish additional information. It may also call upon its experts to examine the taxpayer's books. If the enterprise does not comply with the requests of the administration or answer its questions, or if it does not produce the necessary evidence in support of its statements, the authorities may assess tax *ex officio* on the basis of whatever information they possess.

(2) *Empirical Methods.*

Taxable income is, in principle, determined by the method just described, and recourse is only had to the turnover in order to check the results shown in the accounts. Under the convention with Austria, however, profits are apportioned on the basis of turnover.

(3) *Method of Fractional Apportionment.*

The principle that the profits of the Czechoslovak establishment of a foreign enterprise shall be determined on the basis of the establishment's accounts is subject to certain exceptions. But, as regards the special tax on profits, the law lays down a number of additional rules; if a foreign enterprise has an establishment in Czechoslovakia which sells or buys goods bought or intended for sale abroad, at least half of the total profit from these buying and selling transactions shall be taxable; should the establishment manufacture goods which are sold abroad, at least two-thirds of the total profits from these operations of manufacture and sale will be taxable.

The convention concluded with Austria, however, contains other rules of apportionment (see pages 113 and 114).

(4) *Requirements for Selection of Methods and Value of the Various Methods.*

Apart from the conventions concluded with Austria and Poland, there is no law or treaty clause which prescribes the methods of apportionment to be used. In practice, therefore, the method is adapted to the circumstances of the case. The position of an enterprise is determined as accurately as possible on the basis of the actual circumstances peculiar to each of them. Although this method has undoubted advantages, its application obviously involves many difficulties. Some of these are of a general character, due to the complexity and variety of the methods and forms of commercial organisation, so that it is not always easy to ascertain the exact facts on which taxation is to be based. Other difficulties arise from the accounts, for foreign enterprises frequently try to

escape local taxation by recourse to fictitious accountancy. It is also difficult sometimes to avoid double taxation owing to the numerous and substantial divergencies between national legislation and the laws of foreign countries.

It was thought at one time that the so-called "schematic" method—*i.e.*, the method of taxing a certain fraction or percentage of the total profits of the enterprises as adopted under the Austro-Czechoslovak convention — would avoid these difficulties ; but experience has shown that the main purpose — the avoidance of double taxation — has not been achieved. The two countries do not apply the same rules for assessing taxable income — *i.e.*, computing the gross income and fixing the charges and expenses deductible therefrom. Hence, long negotiations are required in order to agree on the sum to be apportioned fractionally ; or, if each country applies the apportionment fraction to a different sum, a certain measure of double taxation is inevitable.

It therefore still remains to be decided whether any method can be devised which will be at the same time more convenient and more exact. This is true, not only of branches of foreign enterprises, but of subsidiary companies which, if in law independent, in fact form a single economic unit with their parent company.

(c) APPORTIONMENT BETWEEN BRANCH AND PARENT ENTERPRISE.

(1) *Apportionment of Gross Profit of Local Branch to Real Centre of Management abroad.*

No profits of a branch in Czechoslovakia are ascribed either in law or in fact to the enterprise's real centre of management abroad.

(2) *Apportionment of Expenses of Real Centre of Management to Branch.*

Interest Charges.

Interest on debts contracted by a foreign enterprise is not deducted from the profits of the Czechoslovak branch, unless it is shown that the debt is economically connected with that establishment. Such deduction is commonest when the debt is a mortgage debt secured on immovable property belonging to the branch in Czechoslovakia. Mostly, however, this deduction is a question to be determined in each separate case, and there are no general rules for the allocation of these interest charges.

As regards, however, the special tax on profits, the law provides that legally deductible expenses, which include interest charges, must be allocated in proportion to gross income, except when it is possible to determine exactly and directly the receipts to which these expenses correspond.

General Overhead.

What has been said about interest charges applies also to general overhead, and there are no fixed rules of apportionment except in the cases mentioned above.

(3) *Apportionment of Net Profit.*

Of Branch to Deficitary Parent.

Except in so far as the law and the treaties make provision for taxable minima in connection with operations conducted by the foreign enterprise and its Czechoslovak establishment, the latter is taxed without reference to any loss sustained by the parent enterprise. The reason for this is that, from the fiscal point of view, the establishment in Czechoslovakia is an independent national enterprise.

Of Parent to Deficitary Branch.

Subject, again, to the provisions in the law and the treaties concerning taxable minima, the fiscal authorities are only interested in the results of the Czechoslovak establishment. If the accounts of the branch show a loss, there is either no tax or tax is assessed at the minimum figure, as the case may be.

(d) APPORTIONMENT BETWEEN PARENT ENTERPRISE AND SUBSIDIARY.

Subsidiaries are regarded, both fiscally and legally, as independent units, and, for purposes of assessing the taxable income of the branch, only the branch's own profits are taken into account.

II. APPLICATION OF THE METHODS OF ALLOCATION IN SPECIFIC CASES.

*(a) INDUSTRIAL AND COMMERCIAL ENTERPRISES.**(1) Selling Establishments.**Local Establishments selling in National Markets.*

The administration follows no special method in these cases, but determines the branch's income independently.

The special provisions applying in virtue of the conventions to Czechoslovak establishments of Polish and Austrian enterprises were referred to above. As regards Austria, the profits of the establishment from the sale of the products of the foreign enterprise are deemed to be one-third of the total profit from the establishment's turnover, or, if it also makes purchases, the taxable proportion of profits is half. The same applies when the enterprise buys in one country and sells in another.

Local Establishments selling abroad.

The profits earned by an establishment in Czechoslovakia from sales in a country where the enterprise has no establishment are taxable in Czechoslovakia in their entirety, this being regarded as a case of an enterprise within the country extending its operations to a foreign country without having any establishment there. No part of profits is ascribed to the parent enterprise or to the real centre of management.

(2) Manufacturing Establishments.

If a foreign enterprise manufactures goods in its Czechoslovak establishment and sells them in a foreign country where it has no sales office, the total profit from its operations will be taxed in Czechoslovakia. But, if the enterprise has a selling establishment abroad, the share of profits belonging to that establishment will be liable to the general or special profits tax in Czechoslovakia, only if the establishment is liable to no similar tax abroad. (As regards income tax, the exemption is further dependent upon reciprocity.)

Moreover, in the case of enterprises liable to the general tax on profits, at least one-quarter of the total profits from manufacture and sale is held to tax in Czechoslovakia. In the case of enterprises liable to the special tax on profits, the taxable minimum is two-thirds of total profits.

These provisions do not apply to operations carried on in countries with which Czechoslovakia has concluded conventions (the contents of the conventions were indicated on pages 113 and 114).

(3) *Processing Establishments.*

Processing establishments situated in the country are liable to tax. The profits from their activities are assessed according to the method best suited to the particular case.

(4) *Buying Establishments.*

Enterprises which have a buying establishment in Czechoslovakia are liable to tax there. The taxable minimum in the case of enterprises liable to the general tax on profits is one-quarter of the total profit from purchases and sales ; in the case of enterprises liable to the special tax on profits, the taxable minimum is half the total profit.

Enterprises belonging to a country with which Czechoslovakia has concluded a double-taxation convention are subject to the provisions of those conventions instead of to the foregoing rules. The convention concluded with Austria stipulates that the total profit from purchase and sales offices is to be allocated equally between the two countries. According to the convention with Poland, the profits made in one country from the sale of goods bought in the other, and the expenses corresponding to that income, are, in principle, to be allocated in equal parts between the establishments concerned in these operations.

(5) *Research or Statistical Establishments, Display Rooms, etc.*

Every establishment or place of business which a foreign enterprise possesses in Czechoslovakia is liable to tax. By "establishment" is to be understood any permanent installation which in any way whatever, directly or indirectly, enables the operations of an enterprise to be conducted in a given place. An establishment, to be taxable, need not be a direct source of profit ; it is enough that it serves to further the activities of the enterprise to which it belongs. Thus, permanent installations which are in themselves unproductive, but which render the enterprise certain services, constitute establishments. No special methods, however, are prescribed for assessing their profits.

(b) OTHER KINDS OF ENTERPRISE.

Czechoslovak law prescribes no special method of determining the income of establishments of banks, insurance companies, transport enterprises, power, light, and gas enterprises, telephone and telegraph companies, mining enterprises, etc., situated in Czechoslovakia.

The convention concluded with Austria, however, has a clause relating to the taxation of credit institutions and insurance companies, the terms of which were indicated above.

B. NATIONAL ENTERPRISES WITH BRANCHES OR SUBSIDIARIES ABROAD.

I. GENERAL METHODS OF ALLOCATION.

As already mentioned in connection with the special and general taxes on profits, national enterprises which do business abroad without having any foreign establishments are liable to tax in respect of the profits from this business in the same way as in respect of all their other profits.

Enterprises with establishments abroad are, in principle, liable in respect of the profits of such establishments, only if the latter are not being required to pay income tax abroad. In the event of taxation, the same rules of apportionment apply to national enterprises as to foreign enterprises with establishments in Czechoslovakia. In all cases, however, a certain minimum percentage of the foreign establishment's profits will be held to tax in Czechoslovakia.

II. ALLOCATION OF PROFITS TO REAL CENTRE OF MANAGEMENT WITHIN THE COUNTRY.

For purposes of the taxes on profits, the real centre of management is to be considered as an establishment, as it constitutes an organisation which renders services to the business.

As regards enterprises liable to the general tax on profits which have an establishment abroad, the law lays down that at least one-quarter of the enterprise's total profits shall be held to tax in Czechoslovakia.

In the case of enterprises liable to the special profits tax, the rule is that the minimum taxable in Czechoslovakia shall be one-tenth of total profits. Further, when enterprises buy in Czechoslovakia and sell abroad or *vice versa*, at least one-half of the profits from these operations shall be taxable in Czechoslovakia. When enterprises manufacture in Czechoslovakia and sell abroad, the taxable minimum is one-third of the profit from these transactions.

C. TRUST AND HOLDING COMPANIES.

There are no special rules for trust and holding companies. Holding companies having their head office in Czechoslovakia and controlling foreign subsidiaries are treated as described under B, I (page 118). Czechoslovak subsidiaries under the control of foreign holding companies are taxed according to the rules described under A (b) (1) (page 115).

Annex.

TABLE OF TARIFFS.

I. INCOME TAX.¹

i. Normal Rate.

Scale	Amount of taxable income (in Czechoslovak crowns)		Percentage applicable to the total income	Sum to be deducted from the amount resulting from the application of the percentage ²
	Between	And		
I	0	6,000	I	0
2	6,000	8,000	2	60
3	8,000	13,000	3	140
4	13,000	30,000	5	400
5	30,000	40,000	6	700
6	40,000	60,000	7	1,100
7	60,000	80,000	8	1,700
8	80,000	90,000	10	3,300
9	90,000	110,000	11	4,200
10	110,000	130,000	12	5,300
11	130,000	180,000	13	6,600
12	180,000	320,000	14	8,400
13	320,000	460,000	16	14,800
14	460,000	650,000	18	24,000
15	650,000	1,200,000	20	37,000
16	1,200,000	2,000,000	22	61,000
17	2,000,000	2,800,000	24	101,000
18	2,800,000	3,400,000	26	157,000
19	3,400,000	5,000,000	27	191,000
20	5,000,000	and over	29	291,000

¹ Paragraph No. 18 of the Law No. 76, of June 15th, 1927.

² In Czechoslovak crowns.

2. *Temporary Surtax.*¹

Amount of taxable income (in Czechoslovak crowns)		Percentage applicable to the amount of the normal tax
Between	And	
0	15,000	0
15,000	25,000	30
25,000	40,000	40
40,000	60,000	50
60,000	100,000	60
100,000	150,000	70
150,000	300,000	80
300,000	500,000	90
500,000	and over	100

II. GENERAL TAX ON PROFITS.²

	Percentage
Income lower than 4,000 crowns (on condition that the total income of the taxpayer, or of the head of the family in which the taxpayer lives, does not exceed the taxable minimum for the purpose of the income tax).	Not applicable ³
Income not exceeding 7,000 crowns (subject to the restrictions mentioned above).	0.125
Income not exceeding 15,000 crowns.	0.25
Income exceeding 15,000 crowns :	
For the slice between 0 and 30,000.	0.5
For the slice between 30,000 and 140,000.	2.5
For the part of the income over 140,000	4.0

III. SPECIAL TAX ON PROFITS.⁴

I. Ordinary Tax.

	Percentage of taxable profits
(a) Normal rate ⁵	9

¹ Law No. 177, of November 28th, 1931, as amended by Law No. 120, of July 15th, 1932.

² Paragraph 57 of the Law No. 76, of June 15th, 1927.

For taxpayers whose profession chiefly consists in the rendering of personal services and cannot be carried out through an agent (such as lawyers, doctors, artists, writers, etc.), the rates of tax are to be increased by 20 per cent.

³ Although the tax is not levied in this case, it is all the same computed in order to obtain a theoretical basis on which may be determined the surtaxes collected on behalf of the provinces, districts or communes. In so far as enterprises whose capital exceeds 100,000 crowns are concerned, the tax may never be less than one-half per thousand of their capital.

⁴ Paragraph 83 of the Law No. 76, of June 15th, 1927, as amended by Article 2 of the Law No. 167, of November 27th, 1930.

⁵ For minimum rates, see page 102.

	Percentage of taxable profits
<i>(b)</i> Rate applicable to agricultural and producers' co-operatives :	
For the slice between 0 and 20,000 crowns	2
For the slice between 20,000 and 50,000 crowns	3
For the slice between 50,000 and 100,000 crowns	4
For all amounts over 100,000 crowns	5
<i>(c)</i> Rate applicable to savings banks, welfare and educational establishments :	
For the slice between 0 and 20,000 crowns	1
For the slice between 20,000 and 50,000 crowns	2
For the slice between 50,000 and 100,000 crowns	3
For all amounts over 100,000 crowns	4
<i>(d)</i> Rate applicable to mutual insurance companies :	
One per mille of the total net premiums received.	

2. *Excess Profits Surtax.*

<i>(a)</i> Rate applicable to share companies, limited partnerships with share capital, mining companies, partnerships with limited liability :	
For profits between 6 and 8 per cent of the statutory capital	2
For profits between 8 and 10 per cent of the statutory capital	3
For profits between 10 and 12 per cent of the statutory capital	4
For profits between 12 and 14 per cent of the statutory capital	5
Over 14 per cent of the statutory capital	6
<i>(b)</i> Rate applicable to agricultural and producers' co-operatives :	
For profits between 6 and 8 per cent of the corporate capital	2
For profits between 8 and 10 per cent of the corporate capital	3
Over 10 per cent of the corporate capital	4

3. *Liquidation Surtax.*

Four per cent of the corporate excess as existing at the time the enterprise is put into liquidation.

IV. LAND TAX. ¹

Forests : 2 per cent of the cadastral income multiplied by 20, plus 1½ per cent as special increase.

Other land : 2 per cent of the cadastral income multiplied by 17, plus 1½ per cent as special increase.

¹ Paragraph 105 of Law No. 76, of June 15th, 1927.

V. TAX ON BUILDINGS.

1. *Tax on Rents.*¹Percentage of the
rents or rental value

Prague, Brno, Bratislava.	12
Other localities	8

2. *Classified Tax.*²

Category of the building	Number of rooms	Amount of tax (in Czechoslovak crowns)
I	1	5
II	2	10
III	3	15
IV	4-5	30
V	6-7	50
VI	8-9	70
VII	10-11	90
VIII	12-13	120
IX	14-15	150
X	16	170
	For each further room	20

VI. TAX ON CAPITAL YIELD.³

Per cent

1. When the tax is paid directly	3
2. When the tax is paid by withholding at the source :	
(a) Normal rate	6
(b) Special rates :	
Annuities paid as compensation for the taking over of certain enterprises by the State.	10
Interest on bonds issued by public corporations which are authorised to levy surtaxes	4
Interest on savings deposits with agricultural or producers' co-operatives, mutual mortgage banks, etc	3
Interest on mortgage bonds and debentures issued by mortgage banks and savings banks, etc.	1

¹ Paragraph 156 of Law No. 76, of June 15th, 1927.² Paragraph 162 of Law No. 76, of June 15th, 1927.³ Paragraph 179 of Law No. 76, of June 15th, 1927.

VII. TAX ON DIRECTORS' PERCENTAGES. ¹1. *Normal Tax.*

Ten per cent of the percentage, if the total amount of such percentage distributed by the company exceeds 5,000 crowns.

2. *Temporary Surtax.*

Percentages distributed by a company are subject to a surtax of 100 per cent of the normal tax when they are in excess of 50,000 crowns, but not of 150,000 crowns; when they exceed the latter sum, the surtax amounts to 150 per cent of the normal tax.

VIII. TAX ON HIGH SALARIES. ²

Three per cent of salaries in excess of 100,000 crowns per year.

IX. SURTAXES COLLECTED ON BEHALF OF PUBLIC CORPORATIONS OTHER THAN THE STATE. ³

The general and special taxes on profits, taxes on buildings, on land, on capital yield and on high salaries are subject to surtaxes collected on behalf of the provinces, districts and communes. The maximum of these surtaxes is determined as follows :

	Percentage of the basic tax
1. Provincial surtaxes	160
2. District surtaxes	150
3. Communal surtaxes	250
Exceptionally.	350

Further, the taxes are subject to a 7 per cent increase representing the sanitary surtax, which is collected by the State, and in the Province of Bohemia there exists also a school-tax amounting to 10 per cent.

The taxes on profits are also subject to surtaxes in favour of the chambers of commerce, whose rates vary up to 15 per cent of the basic tax.

¹ Paragraph 183 of Law No. 76, of June 15th, 1927.

² Paragraph 184 of Law No. 76, of June 15th, 1927.

³ Law No. 77, of June 15th, 1927; Law No. 169, of November 27th, 1930.

FREE CITY OF DANZIG

BY

FRITZ LADEMANN,

Counsellor of State, Head of the Fiscal Administration.

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PART I. — GENERAL DESCRIPTION OF INCOME-TAX AND PROPERTY-TAX SYSTEM.¹

In the Free City of Danzig, the taxes levied by the State upon income and property are : income tax proper ; company tax ; business tax ; property tax ; and tax on fixed salaries.²

Income tax (Einkommensteuer) is imposed upon the total income of individuals.

Company tax (Körperschaftsteuer) is levied on the income of companies and other legal entities.

These two taxes are supplemented by a temporary *emergency surtax (Notzuschlag)*. All individuals and legal entities are liable to this supplement, if they pay income tax or company tax. The only exceptions are taxpayers who are liable to income tax on their salaries or wages and whose income from this source does not exceed 100 florins a month.

Tax on fixed salaries (Festbesoldetensteuer) is levied only upon the salaries and wages of officials, employees and workmen in the service of the State and of Danzig public corporations and institutions. Being of limited importance, it will be left out of account in the present survey.

Business tax (Gewerbesteuer) is imposed upon legal entities as well as upon individuals and is levied on all profits from the carrying-on of profit-making activities in an establishment situated within the Free City.

Property tax (Vermögensteuer) is levied on the property of all individuals and legal entities liable to income tax or company tax.

The various taxes dealt with in this survey are governed by the following legislative provisions :

Law of December 31st, 1931 (*Law Bulletin* No. 4 of 1932), as regards income, company, property and business taxes ;

Decree of September 26th, 1931, as amended on December 9th, 1931, and June 28th, 1932 (*Law Bulletin* Nos. 50 and 66 of 1931 and No. 42 of 1932), as regards the emergency surtax ;

Decree of January 30th, 1931, and amendments of March 7th, September 25th and October 13th, of same year, as regards the tax on fixed salaries ;

Organic law (*Steuergrundgesetz*) of June 22nd, 1931 (*Law Bulletin* No. 28 of 1931), which contains provisions common to all the taxes and for the most part settles questions relating to administration, procedure and appeals.

I. INCOME TAX.

I. TAXPAYERS.

Only individuals are liable to income tax (*Einkommensteuer*). General partnerships, joint ventures and *de facto* associations do not constitute taxable entities, while legal entities are liable to the special tax known as company tax (*Körperschaftsteuer*).

¹ Legislation in force on March 31st, 1933.

² According to the budget estimates for 1932, direct taxes are expected to yield 49,316,500 florins, of which income tax and company tax should furnish 24,200,000; property tax, 2,000,000; and tax on business and industry, 4,000,000.

The Customs administration, which collects, not only Customs, but consumption duties, the stamp duty and monopolies, estimates its receipts at 27,316,500 florins, made up as follows : Customs, 7,000,000 ; consumption duties, 10,000,000 ; stamp duty, 4,239,000 ; monopolies, 6,677,500.

The income-tax law distinguishes between taxpayers with an *unlimited tax-liability* — i.e., persons taxable in respect of all their income of whatever origin — and taxpayers with a *limited tax-liability* — viz., persons who are liable only in respect of income originating in the Free City, or, in other words, their Danzig income (for details see under "Taxable Income" below).

An unlimited tax-liability attaches to all individuals who are domiciled or normally resident in the Free City. Residence is normal if it extends beyond six months and, in such case, liability extends also to the first six months.

Officials of the Free City occupying posts abroad have also an unlimited tax-liability.

According to the fiscal law of Danzig, a person is domiciled in the Free City if he occupies a dwelling there in circumstances that imply an intention to retain it. Normal residence is the place where he is residing under conditions which imply an intention to make more than a temporary stay in the place or country.

2. TAXABLE INCOME.

Let us now examine in turn the income taxable :

- (a) Against individuals with an unlimited tax-liability ;
- (b) Against individuals with a limited tax-liability.

(a) *Unlimited Tax-liability.*

Individuals subject to an unlimited tax-liability pay tax on the whole of their income, irrespective of its origin.

The term income includes :

(1) *Income from the Exploitation of Land and Forests.* — This comprises income from agriculture and forestry, profits from market-gardening and fruit-growing, from stock-breeding, nursery-gardens, pisciculture and fishing, sand pits and quarries ;

(2) *Income from Business and Industry.* — This class of income includes, not only the profits from an enterprise the sole owner of which is the taxpayer himself, but the salaries, remuneration and shares of profits which the taxpayer receives as a member of a partnership, or as a general or managing partner in a limited partnership, with or without share capital, whether in consideration of his work or the capital brought by him into the business, except, however, in the case of limited partnerships, income from assets making up part of the statutory capital.

Income from business and industry further comprises profits from the sale or cession of all or part of a business or industry and partners' shares in partnerships or the shares of managing partners in limited partnerships. In these cases, however, the profits are not taxed unless they exceed 1,000 florins.

(3) *Income from Independent Professional Activities.* — This heading includes all profits from independent professions that cannot be grouped in one of the foregoing categories — e.g., the income of doctors, barristers, notaries, consulting engineers, architects, etc., and the remuneration of directors, auditors, etc., of the different commercial companies.

(4) *Remuneration for Work done in the Service of Another.* — This group includes salaries, wages, shares in profits, bonuses, etc., paid to employees or workmen working on another's behalf, and the pension granted to the worker himself or to his widow and orphans in consideration of past services.

(5) *Income from Capital.* — Income of this kind includes dividends, interest and various advantages attaching to the possession of shares issued by legal entities, limited liability companies, etc., income accruing to sleeping partners, interest on bonds and loans of all kinds, etc.

When dividends and similar income are received by companies subject to an unlimited tax-liability in Danzig, they are only taxable to the extent of 70 per cent in the case of income received from share companies or limited partnerships with share capital, and to the extent of 50 per cent in the case of income from limited liability companies.

(6) *Income from the Lease or Rent of Real Estate and Intangible Personal Property.* — Under this category are grouped rents of farms, land and buildings, proceeds from chartering ships registered in Danzig, annuities from rights in real estate, from the goodwill and other accessories of businesses, royalties from patents and copyrights, provided that these royalties cannot be regarded as part of the profits of an independent profession.

(7) *Various Periodical Income.* — Included in this class are annuities of all kinds received in consideration of the payment of a capital sum.

(8) *Miscellaneous Gains.* — This class includes income from activities not coming under Nos. 1 to 4, especially profits from casual transactions and from the lease of tangible personal property, including unregistered vessels.

Casual sales are taxable if effected for speculation. Such intention is presumed in the case of a sale of landed property, when the interval between purchase and sale is less than two years ; as regards other property, particularly securities, when the interval is less than six months.

These operations are not, however, taxable if the taxpayer can show that the purchase had no speculative purpose or that the article sold is not part of the seller's taxable property or when the profits from sales of this kind effected during the year amount to less than 500 florins.

(b) *Limited Tax-liability.*

Persons with a *limited tax-liability* pay tax on the following income :

- (1) Income from agricultural and forestry exploitations situated within the territory of the Free City ;
- (2) Income from a business or industry having an establishment or a permanent representative within the Free City ;
- (3) Income from the lease or rent of real estate, tangible personal property situated within the territory of the Free City, or rights registered in a public register of the Free City ;
- (4) Income from any independent profession carried on within the Free City ;
- (5) Income from salaried employment which is or has been accomplished in the Free City ;
- (6) Dividends, interest, royalties and other income from shares in Danzig limited liability companies ;
- (7) Income accruing to a sleeping-partner in a Danzig business ;
- (8) Profits from the sale of Danzig real estate or of rights to real estate ;
- (9) Regularly recurring receipts from Danzig public funds paid in consideration of present or past services, in so far as these are not taxed under (5).

3. ASSESSMENT OF TAX.

(a) *Computation of Taxable Income and Deductions.*

Taxable Amount. — Tax is levied upon the total income which the taxpayer has received within the taxable period. The taxable period is, in principle, the calendar year preceding the

year for which tax is assessed. In the case of taxpayers who keep books in conformity with the Commercial Code, it is the business year ending in the course of the calendar year for which the tax is computed.

Income is deemed to have been received within the taxable period during which it became due or, without being due, was actually paid to the taxpayer.

In the case of taxpayers who regularly draw up a profit-and-loss account, income is deemed to have been received within the latest fiscal period for which the principles of good book-keeping allow of its being entered in the accounts. Taxable income is gross income less deductible expenditure.

In the case of taxpayers who do not keep accounts and are not obliged to do so, gross income consists of their actual receipts.

If, on the other hand, a taxpayer keeps accounts, whether obliged to do so or not, account must be taken, not only of income actually received (in cash or in kind), but of any appreciation of assets, determined by a comparison of the balance-sheet for the taxable year with the balance-sheet of the previous year.

The following constitute deductible expenses :

(1) The cost of earning the income — *i.e.*, all expenses incurred in producing, maintaining, ensuring and collecting the said income.

The deductible expenses of business and industries include rents, wages, cost of goods to be worked up, cost of upkeep, salaries and wages of employees and workmen, depreciation, insurance premiums, etc., paid by the enterprise or deducted from its profits. These expenses do not include sums devoted to adding to or improving the taxpayer's property or business or the paying of his debts.

The cost of purchasing articles necessary to the taxpayer's business may not all be deducted from the profits of the year in which the goods were purchased. Deduction must be in proportion to the lifetime of the goods — that is to say, the amount to be deducted each year will be the sum obtained after dividing their price by the number of years they will remain in use.

Machinery, tools, etc., buildings, drainage systems, trade marks, patents, etc., must be written off annually at a percentage rate corresponding to the lifetime of the article. The depreciation allowances must not exceed the price of purchase or replacement. It is also permitted to build up reserves to meet the gradual depletion of sand pits and quarries.

- (2) Taxes paid on real estate, business and industry and other public contributions.
- (3) Insurance premiums, in so far as they are to be regarded as expenditure necessary to the enterprise.
- (4) Interest on debts contracted by the taxpayer and other annual charges he is required to meet.
- (5) Travelling expenses of the taxpayer from his home to his place of work.
- (6) Cost to workmen and employees of buying tools and working clothes.
- (7) Cost of clearing and draining land, etc.
- (8) Certain expenses unconnected or not directly connected with the earning of income :

(a) Provided they do not exceed 1,200 florins in all and, eventually, the sum that may be fixed for each item : contributions paid by the taxpayer in respect of himself or his dependents to pension funds for widows and orphans, insurance funds against sickness, accidents, liability, disablement and unemployment ; contributions to mutual benefit

societies to cover funeral expenses, provided these contributions do not exceed 100 florins a year ; life insurance premiums to insure the lives of the taxpayer or his dependents, provided the annual payments are not above 1,200 florins ; deposits with Danzig savings banks, if it is stipulated in an irrevocable manner that their repayment in the event of death will not be made to the taxpayer or surviving dependents until after ten years, and if the payments do not exceed 12,000 florins a year ; contributions to trade unions or professional organisations recognised by administrative law and to other professional associations with no purpose of gain ;

(b) Without restriction of amount : contributions to religious bodies, sums paid into pensions or relief funds belonging to the taxpayer's enterprise, provided these are permanent funds ; expenses incurred by the taxpayer in improving his professional capacities.

Although the income of each of the classes enumerated (see " Taxable Income " above) is separately computed, it is permissible to deduct from the total income losses on income of a specific class. The same applies to expenses not connected with any special class of income.

In the case of taxpayers with a limited tax-liability, only those expenses may be deducted which relate to income taxable in the Free City. When persons with an unlimited tax-liability are, for one reason or another (see page 142), not liable to tax on certain foreign income, they may not deduct from the taxable sum expenses connected with such untaxed income.

Returns. — The following must make a return of income :

- (1) Anyone required to do so by the fiscal administration ;
- (2) Anyone in receipt of an income exceeding 10,000 florins ;
- (3) Anyone in receipt of Danzig income (see page 130, paragraph (b)), but not domiciled or normally resident in the Free City.

Taxpayers who are domiciled abroad but have taxable property, a branch or place of business, or are liable to pay taxes within the territory of the Free City, must, when requested by the Administration, appoint a *representative* in the Free City authorised to receive notices on their behalf. If they omit to do this, a notice will be deemed to have been served upon them as soon as it is registered and posted, even if it is returned to sender " address unknown ".

Verification. — The taxpayer must furnish the fiscal Administration orally or in writing with information which, to the best of his knowledge, is true ; he must, on request, produce evidence in support of his tax return if his statements are open to reasonable doubt ; he must, also on request, submit, for inspection and checking, books, accounts and other documentary data required for purposes of tax assessment. Taxpayers who keep accounts according to the Commercial Code must, if requested, produce full copies of their balance-sheets, with explanations, and a copy of their profit-and-loss account.

With the exception of immediate relatives, even persons who are not taxpayers may be required to furnish reliable information on facts of material importance for tax assessment, and, if necessary, to submit books and documents.

The Administration may further have recourse to experts, who may be called on to co-operate with the inspectors belonging to the Administration, and to the representatives and agents of the associations and groups representing the branch of industry or business to which the taxpayer belongs.

The fiscal authorities may, if they have good reasons for so doing, examine whether the books and accounts of a taxpayer are complete, regular and, in form and substance, properly kept. This inspection of books is carried out by a specially trained staff of fiscal agents, and may extend to all matters of possible importance for purposes of computing tax.

Properly kept books and accounts form the normal basis of assessment. If the fiscal administration is unable to determine or compute income on that basis, it must make an estimate in the light of all the evidence at its disposal, particularly when the taxpayer is unable to furnish adequate explanations in support of his statements or refuses further information. The same procedure is adopted when the taxpayer is unable to produce the books or accounts he is required by fiscal law to keep, or when such books and accounts are incomplete or incorrect as to form or substance,

Once an assessment is made, the administration delivers a notice to the taxpayer. In the case of income tax, no assessment is made if the income consists entirely of income taxed at source (see page 134), or if the income does not exceed a certain figure.

Appeals. — A taxpayer has the following remedies against his tax assessment : recourse to the fiscal administration itself ; appeal against the administration's decision to the Fiscal Chamber of the Administrative Court and, against the latter's judgment, to the Supreme Administrative Court.

Instead of protesting to the administration, appeal may be made direct to the fiscal chamber of the administrative court of second instance, if the head of the administration gives his consent. As a rule, appeals to the Supreme Administrative Court are only made when the amount of tax in dispute exceeds 100 florins.

Other cases — for instance, those dealing with tax payments, fines, etc. — are normally decided by the fiscal administration itself.

(b) *Computation of Tax and Deductions.*

1. *Income Tax Proper.* — There are three rates of tax, the ordinary rate, the special rate for directors' percentages and the rate applying to salaries and wages. The first two are graduated, but not the third. The different rates are reproduced in an annex.

Before applying the ordinary rate and the rate applicable to salaries and wages, certain sums have, however, to be deducted from the taxable income, representing the tax-free minimum and certain flat-rate deductions on the score of professional expenses and allowances for dependents.

The deductions allowed in the form of a tax-free minimum or on the score of dependents are, under the ordinary rate of tax, as follows :

	Florins a year
For the taxpayer himself	240
For his wife, if unable to earn her own living	120
For one child, if dependent on the taxpayer	120
For the first of several children	600
For second child	720
For third child	840
For fourth and each subsequent child	1,440

As regards salaries and wages, the taxable sum is reduced by the following deductions on the score of professional expenses and dependents :

	Florins a month
Unmarried persons	60
Married persons without children	90
Unmarried or widowed persons with one child	90
Married persons with one child	100
Unmarried or widowed persons with two children	190
Married persons with two children	200
Unmarried or widowed persons with three children	260
Married persons with three children	270
Unmarried or widowed persons with four children	380
Married persons with four children	390

2. *Emergency Surtax.* — Income and company tax are temporarily liable to a special emergency surtax. This surtax is payable by all individuals personally liable to income tax. Exemption is granted to persons whose income from their work is taxed at the source and whose salary or wage does not exceed 100 florins a month. Taxpayers are further exempt from the emergency surtax if their annual income does not exceed 600 florins.

Whenever the net income of a taxpayer is less than 5 per cent of his property, as valued on December 31st of the preceding year, the emergency surtax will be assessed, not on the income, but on one-twentieth of the property, the rates of tax being unchanged.

The scale of the emergency surtax is reproduced in an annex to this study.

4. COLLECTION OF TAX.

Only salaries and wages are taxed at the source. The tax is deducted by the employer at the time of paying the wage or salary and has to be handed over by him to the Administration.

In the case of all other income, tax is paid in four quarterly instalments, the first of them on February 15th.

Payments made before receipt of the assessment notice must be made on the basis of the previous year's tax and if, when the assessment notice is received, the amount due is found to exceed the amount on the basis of which previous payments were made, the difference must be made good within a fortnight.

II. COMPANY TAX.

I. TAXPAYERS.

Subject to the exemptions specified below, company tax is imposed on all commercial companies, such as share companies, limited partnerships with share capital, limited liability companies, or other legal entities under private law, associations whether or not formed for purposes of gain (which are not legal entities); foundations and special estates (*Zweckvermögen*), in so far as the income is not subject to the company tax or the income tax directly in the hands of another taxpayer. Company-tax law, like income-tax law, distinguishes between a limited and an unlimited tax-liability. A company or legal entity having its head office or centre of management in the Free City has an unlimited tax-liability. The liability is limited in the case of foreign companies in receipt of income which is regarded as Danzig income within the meaning of the income-tax law. A company's head office is in the place designated as such by the statutes or articles of association. The centre of management is the place from which the enterprise is controlled.

Exemptions.

The following companies and legal entities are exempt from this tax :

(1) Companies which are not engaged in trade or industry, but hold shares in other companies, Danzig or foreign, and whose only function is to administer and manage those securities (holding companies) ;

(2) The Bank of Danzig ;

(3) Public savings banks and, under certain conditions, private savings banks ;

(4) Co-operative societies belonging to a union of co-operatives trading exclusively with their members and whose business consists only of the retail sale of commodities for current use ;

(5) Unions of such co-operatives, provided, of course, that they only deal with co-operative societies making up the union ;

- (6) Mutual insurance companies doing business with their members only ;
- (7) Companies and legal entities which, under their statutes, confine their activities to religious purposes, charities, or public welfare.

2. TAXABLE INCOME.

What was said above (about taxable income) in connection with income tax applies also to company tax, both when the tax liability is limited and when it is unlimited. If, however, companies can show that they have, from the beginning of the year for which assessment is being made, held one-fifth of the capital of another company in the form of shares of one kind or another, the income from these shares will not be taxed. Contributions paid to associations (*Personenvereinigungen*) by their members are likewise not taxable.

3. ASSESSMENT OF TAX.

(a) *Computation of Taxable Income and Deductions.*

Taxable Amount. — Before profits can be taxed, they must have been earned ; it does not matter whether they have or have not been distributed among the shareholders and members of the company. Profits are normally assessed and computed by the same rules as apply to income tax.

Deduction must, however, be made of the items deductible for purposes of income tax. These are :

(1) The benefits of all kinds accruing out of the profits of the tax year either to members of the Board of Directors, on condition that their functions are not confined to mere supervision and control — that is, to directors and managing partners really responsible for the conduct of the enterprise — or to employees and workmen in payment for their work, provided, of course, that such payments have not already been deducted as part of working costs ;

(2) The benefits accruing to general partners of limited partnerships with share capital other than the remuneration for capital assets brought into the business and forming part of the firm's capital ;

(3) In the case of commercial companies, the cost of issuing shares and other securities, unless these are covered by issue bonuses ;

(4) In the case of insurance companies, sums taken out of profits to build up reserves in connection with risks insured against ;

(5) Sums set aside under the statutes, articles of association or any other act, for purposes of public welfare and charity.

As in the case of income tax, these deductions from profits are only allowed if they are connected with activities the income from which is taxable. This applies to companies whose tax-liability is limited and to other companies which, for one reason or another, are not liable to tax on certain foreign income.

Returns, Verification, Appeals. — The following must make a return for purposes of company tax :

- (1) Any company or legal entity requested to do so by the administration ;
- (2) Any profit-seeking company and any legal entity under private law liable to company tax and in receipt of an income for the tax year exceeding 1,000 florins ;
- (3) Taxpayers under (2) above who, in the course of the tax year, had their head office, centre of management or an establishment in the Free City, or who have been in receipt of Danzig income (see page 130, paragraph (b)).

The provisions governing the serving of assessment notices, the checking of returns, and appeals are the same for company tax as for income tax (see pages 132 and 133).

(b) *Computation of Tax and Deductions.*

Company tax is always proportional, but its rate differs according as the legal entity or association, which is liable to taxation, is or is not engaged in profit-making activities. The emergency surtax is the same for companies as that which is paid by individuals liable to income tax on income other than salaries and wages (see Annex).

4. COLLECTION OF TAX.

Company tax is always payable by the taxpayer direct ; it is collected at the same date and under the same conditions as income tax.

III. BUSINESS TAX.

I and 2. TAXPAYERS AND TAXABLE INCOME.

Every individual or corporation which has an establishment in the Free City of Danzig and engages in profit-seeking operations is, in principle, liable to pay the business tax (*Gewerbesteuer*). Legal entities are liable in the same way as individuals. Further, partnerships and *de facto* associations which do not constitute taxable entities for purposes of either income tax or company tax (members of such associations being liable individually to income tax on their share of profits) are, in this case, liable.

Nor is any distinction made between an unlimited tax-liability and a limited tax-liability, and the extent of the liability is independent of domicile. Liability to the tax depends, in the first place, upon the existence of an establishment and, in the second, upon the fact that certain activities are there pursued.

By an establishment, the law means any premises or installation serving for the carrying-on of an independent business, conducted by the taxpayer himself or his representative or permanent agent. Among such establishments are : branches, factories, purchase and sale offices, desk-room, stalls and stands in public markets.

Taxable operations include, in principle, all independent businesses, industries and occupations. They do not include agriculture and forestry (unless these undertakings are mainly industrial or commercial), the arts, sciences or literature.

Exemptions. — The following are exempt from this tax :

- (1) The Free City of Danzig, its communes and unions of communes (*Kommunalverbände*);
- (2) Societies, associations and special estates (*Zweckvermögen*), which, under their statutes or constitutions, are devoted exclusively to charitable or public welfare purposes ;
- (3) Subject to certain restrictions, co-operative societies which trade only with their members and distribute no profits.

3. ASSESSMENT OF TAX.

(a) *Computation of Taxable Income and Deductions.*

The taxable sum is, in principle, the same as is determined for purposes of income tax or company tax. To the sums thus obtained, however, must be added the following items :

- (1) Interest corresponding, not to current commitments, but to debts and permanent charges, and paid either to members or to third persons ;

(2) Salaries, percentages and other benefits distributed in any form by a partnership or similar association to its members or by a limited partnership to its general partners as remuneration for services rendered ;

(3) Exceptional bonuses paid by a limited liability or share company to its managers or to members of its Board of Directors. By exceptional bonuses are meant bonuses over and above simple payment for services rendered ;

(4) If the taxpayer exercises his occupation on premises belonging to him, the taxable profit must be supplemented by 4 per cent of the value of these premises as last assessed for purposes of property tax. If only part of the building is used in the exercise of the occupation or if the building has only been so used for part of the year, a proportionate reduction is made.

Assessment procedure returns as well as their checking and appeals are governed by the provisions explained in connection with income tax and company tax.

(b) *Computation of Tax and Deductions.*

There are two methods of computing the tax ; according to the former, tax is not computed on profits, but from certain outward signs, whence is obtained the minimum tax, which is always due even if the concern has not earned a profit, but which, if a profit is earned, is deducted from the tax normally payable.

For purposes of ascertaining the minimum tax, taxpayers are grouped in seven classes, each with a different tax (see Annex), except the seventh class, which is tax-free. The classification is made by the Administration, with due regard for (1) the kind of business ; (2) the rental value of business premises ; (3) the working capital belonging to or borrowed by the taxpayer for the needs of his business ; (4) the size of the staff ; (5) the turnover for the previous year ; (6) receipts for that year.

The tax, the rates of which are annexed, is graduated and is only levied on taxpayers whose profits exceed 2,400 florins a year.

4. COLLECTION OF TAX.

Business tax is collected at the same date and under the same conditions as income tax.

IV. PROPERTY TAX.

I. TAXPAYERS.

Persons who are liable to income tax or company tax are also, as a rule, liable to property tax. Here, again, account is taken of the taxpayer's domicile and a distinction made between persons with an unlimited tax-liability and those whose tax-liability is limited.

2. TAXABLE PROPERTY.

(a) *Unlimited Tax-liability.*

Persons whose tax-liability is unlimited are liable on all the property making up their fortune, wherever it is situated. Such property includes :

(1) Real estate with its appurtenances ; rights subject to the provisions of civil law on real estate, usufruct and other rights on real estate and debts secured on real estate ;

(2) Fixed and working capital employed in agriculture, forestry, business or industry (this covers all objects used in an enterprise, including stocks manufactured or intended for sale) ;

(3) All other capital — in particular, rights and receivables of all kinds, shares in companies or enterprises, cash, precious metals and stones, the capital value of certain annuities and usufructs, and, lastly, life insurance claims not yet due.

The capital value of pensions or annuities paid as allowances or indemnities does not rank as taxable property.

(b) *Limited Tax-liability.*

In the case of persons whose tax-liability is limited, the taxable property consists of real estate in Danzig and capital invested in an agricultural or forestry enterprise, a business or an industry established in the Free City.

3. ASSESSMENT OF TAX.

(a) *Computation of Taxable Property and Deductions.*

Taxable property is assessed, in principle, on the basis of the situation on December 31st of the year preceding the year in which the tax is paid, except in the case of enterprises which keep accounts, for which the date is that of the last balance-sheet.

If during the tax year a taxpayer's property has diminished in value by more than one-fifth or by as much as 20,000 florins, he may apply for a reassessment on the basis of the real value of his property.

The Administration possesses the same right if the taxpayer's property has appreciated by more than one-fifth or by as much as 20,000 florins.

In principle, property is assessed at its intrinsic worth. If property is permanently devoted to a business, assessment may be based, not on its intrinsic worth, but on purchase price, or price of manufacture, if these prices are below current value. The net value of the property is obtained by deducting from its gross value :

- (1) Debts economically connected with the property ;
- (2) The capital value of certain recurrent payments to which the taxpayer is committed — e.g., annuities, etc. ;
- (3) In the case of a taxpayer with an unlimited tax-liability and under certain conditions, certain debts incurred for his private needs for three months ;
- (4) The reserves built up by insurance companies to cover risks, dividend payments, etc. ;
- (5) Reserves, under certain conditions, established for charitable or public-welfare purposes.

When the taxpayer is only liable on part of his property, the deductions are only allowed if they are economically connected with property that is taxable.

The rules of procedure in the matter of returns, control and appeals are the same as in the case of income tax (see pages 132 and 133).

(b) *Computation of Tax and Deductions.*

Property tax is only collected on estate exceeding 10,000 florins in value ; it is a graduated tax (see Annex).

4. COLLECTION OF TAX.

The tax is paid at the same date and under the same conditions as income tax.

PART II. — TAXATION OF FOREIGN AND NATIONAL ENTERPRISES.

A. FOREIGN ENTERPRISES.

I. DEFINITION AND GENERAL PRINCIPLES.

A foreign enterprise is an enterprise belonging to an individual whose domicile is abroad or to a company whose head office or centre of management is not in Danzig.

These enterprises, or rather their owners, have only a limited tax-liability for purposes of income and company tax, as well as property tax.

Enterprises belonging to individuals or to partnerships (general partnerships, limited partnerships, joint-ventures and *de facto* associations) are liable to income tax. In the case of the latter, assessment is made, not against the partnership or association, but against each member, who is individually liable to tax on his share of profits or taxable income.

Enterprises belonging to share companies, limited partnerships with share capital, other companies constituting legal entities within the meaning of Danzig private law, and limited liability companies are liable to company tax.

These enterprises will be further liable to the business tax if they have a business establishment in the territory of the Free City. This tax is levied alike upon individuals, partnerships and companies and, in the case of partnerships, a single assessment is made, contrary to the procedure for purposes of income tax.

Foreign enterprises belonging to individuals, partnerships or companies are also liable to property tax and, as in the case of income tax, their tax-liability is limited — that is, they are only liable on property which is deemed to be situated within the territory of the Free City. Ordinary partnerships are assessed by the same rules as for income tax, which means that a separate assessment is made for each member.

Before considering separately the fiscal treatment of each kind of income that foreign enterprises may derive from the Free City of Danzig, we give the following general survey :

These enterprises are liable on all income from profit-seeking activities exercised in the territory of the Free City, on real property and real property rights or debts secured on such property and rights, and on all capital invested in enterprises situated in the territory of the Free City, *except* :

- (1) Dividends, interest and income from securities proper ;
- (2) Interest on unsecured debt of all kinds ;
- (3) Profits from casual speculation in property other than real estate.

As regards property tax, we may repeat that the only property in respect of which a taxpayer has an unlimited tax-liability is :

- (1) Real estate and real property rights situated in Danzig ;
- (2) Debts secured on such estate and rights ;

(3) The assets of establishments used for profit-making purposes in the Free City.

These rules, however, are subject to certain exceptions provided for in double taxation Conventions concluded with Poland and Germany (for summary of these Conventions, see page 143).

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) *Dividends.*

Dividends from shares issued by Danzig companies are not, as a rule, taxable when they accrue to foreign enterprises. The tax-liability of these enterprises is limited and such income is not included among the income taxable against this class of taxpayer (see page 130).

If, however, these dividends are part of the industrial or commercial profits of an establishment owned by a foreign enterprise in the Free City, they are taxable as income from a business or industry. The same applies if the establishment is in receipt of dividends from foreign companies.

On the contrary, the non-resident is taxable in respect of income from parts in a limited liability company, or from an interest as sleeping-partner in a partnership in Danzig, even if such income is not received at an establishment situated in the Free City.

The capital value of shares will be liable to property tax if the dividends are taxable. Shares of sleeping-partners in partnerships are always taxable.

(b) *Interest.*

Foreign enterprises in receipt of interest pay tax only on interest from loans secured on real estate or property legally situated in Danzig. All other interest is only taxable if it is part of the industrial or commercial income of an establishment situated in the Free City. The capital on which this interest is paid will be liable to property tax, when the interest is liable to income tax or company tax.

(c) *Directors' Percentages.*

Directors' percentages paid by Danzig companies are in all cases taxable.

(d) *Royalties for Use of Patents, Copyrights, Trade Marks, Secret Processes and Formulæ and Similar Income.*

Patent royalties and other intangible rights are taxable if the rights to which they correspond are publicly registered in Danzig, whether they accrue to foreign or to Danzig enterprises. The capital value of these intangible rights will be taxable under the same conditions.

(e) *Rents from Real Estate, Mining Royalties and Similar Income.*

Income derived from the lease or exploitation of real estate situated in Danzig or from any rights to such estate is taxable, and the value of such property and rights is liable to property tax, irrespective of the status of the owner.

(f) *Gains derived from the Purchase and Sale of Real Estate, Securities and Personal Property.*

In the case of foreign enterprises — that is, taxpayers whose tax-liability is limited, only profits from the purchase of real estate in Danzig are taxable. Moreover, the purchase and sale must have been effected with a speculative object and the profit must exceed a certain figure. These different conditions are given in detail on pages 129 and 130.

Transactions in personal property, tangible or intangible, are only taxable if they are among the activities of an establishment situated in the Free City.

(g) *Salaries, Wages, Commissions and Other Remuneration for Services (including Directors' Salaries and Fees).*

Salaries and wages are taxable if they are in payment for services performed in the territory of the Free City. Unlike other cases, income tax on these payments is deducted at the source.

Salaries and wages paid for functions exercised abroad are also taxable, if paid out of Danzig public funds. Further, income tax is differently computed in regard to salaries and wages from the method of computation applied to other income (see page 133).

A tax named *Festbesoldetensteuer*¹ is further levied upon the fixed salaries of persons employed by the State, public corporations, institutions and services in general. Such persons, however, do not pay the emergency surtax levied upon other salaries and wages.

(h) *Income from a Trust.*

Danzig private law does not recognise any institution exactly comparable with the trusts of Anglo-Saxon countries. We may, however, place in this category foundations and special estates (*Zweckvermögen*). These legal entities are, in principle, liable to company tax, but there is no provision for taxing persons with a limited tax-liability in respect of income they derive from any right in such estates or foundations.

(i) *Income from the Carrying-on of a Business or Industry.*

1. *A Local Commission Agent or Broker.* — A foreign enterprise which merely buys or sells through some strictly independent middleman, like a commission agent or broker, cannot be said to have an establishment in the Free City and is therefore not liable to tax.

2. *A Local Dealer or Distributor.* — The same applies when the foreign enterprise sells its goods to a dealer established in the Free City, giving him exclusive rights of re-sale. If, however, the circumstances are such that this dealer is in economic dependence upon the enterprise whose goods he buys — that is, if he is obliged to sell the goods of that enterprise only — to the exclusion of all other goods, the enterprise may be regarded as having a permanent representative in the Free City and be held to tax as such.

3. *A Travelling Salesman, whether or not having Power to conclude a Contract.* — The foreign enterprise is not liable, for it has neither an establishment nor a permanent agent in Danzig and therefore fulfils none of the conditions necessary to be regarded as exploiting a business there.

A commercial traveller, however, comes under the law on the taxation of itinerant trades (*Wandergewerbsteuergesetz*), which lays down that any person engaged in a trade or business in territory of the Free City without having an establishment there must pay what may be considered

¹ See definition, page 128.

as a *licence* tax, the amount of which varies for five different classes, each of them fixed according to certain outward signs, such as the kind of business, the material and staff employed and the nature of the articles sold.¹

4. *A Local Agent with a Power of Attorney.* — A foreign enterprise which has an agent permanently established in the Free City and authorised to bind the enterprise is regarded as liable.

5. The same is true when it maintains in the territory of the Free City *an agent who sells out of stock* entrusted to him by the enterprise.

6. *An Establishment of Any Kind.* — Enterprises having an establishment in Danzig are liable to tax there on all profits held to have been earned by that establishment and on all property belonging to the latter's assets.

By "establishments" are to be understood all permanent installations and all premises used for the exercise of a trade, industry or other business, especially branches, factories and workshops, buying offices and selling stores, warehouses, agencies and other installations serving the purposes just mentioned, whether the activities are exercised by the owners of the enterprise, by proxies or other permanent representatives.

A building enterprise will be regarded as having a permanent establishment in the Free City for purposes of liability to the business tax if its yards are established in the Free City for longer than twelve months.

On the other hand, gas, light and water companies, which merely lay wires or pipes in the Free City, are not regarded as having an establishment there unless they serve consumers established in the territory.

B. NATIONAL ENTERPRISES.

For the purposes of the present survey, a national enterprise is any enterprise belonging to an individual domiciled in the Free City or to a legal entity whose head office or centre of management is in that territory. As mentioned in Part I, these enterprises are subject to an unlimited tax-liability, being liable to tax on all their income, whether derived from abroad or from within the territory.

Although, in principle, the fiscal treatment of foreign and Danzig income is the same, dividends constitute an exception. Dividends paid to Danzig enterprises by foreign companies are taxable to their full amount and benefit by none of the abatements which, with a view to the avoidance of double taxation in Danzig, are allowed in the case of dividends paid by Danzig companies (see page 140). But the principle of unlimited tax-liability does not operate in the case of the *Gewerbesteuer* (business tax), which is in no case levied upon the profits and income of foreign establishments.

The rules outlined above are subject to certain exceptions embodied in Conventions concluded with Poland and Germany, the contents of which are stated below.

C. DOUBLE TAXATION AGREEMENTS.

The Free City has concluded Conventions of this kind with Germany (Decree of November 21st, 1923, *Law Gazette*, page 730, supplemented by Decree of July 31st, 1926, *Law Gazette*, page 275), and with Poland (Convention of May 29th, 1929, Law of May 16th, 1930, *Law Gazette*, page 107).

These two Conventions provide for exemptions, in principle reciprocal, in favour of taxpayers of each of the contracting States. We shall show these exemptions in a table, where, opposite to

¹ Law on the Taxation of Itinerant Trades, *Law Bulletin of the Free City of Danzig*, No. 4 of January 20th, 1932, pages 70 *et seq.*

each kind of income, will appear the rule adopted in each Convention. It is to be understood that if, according to the table, one kind of income is taxable in one country, it is not taxable in the other, and that, when the income in question is derived wholly or partly from capital, the capital is treated in the same way as the income :

Kind of income.	As between Danzig and Germany.	As between Danzig and Poland.
1. Income from agricultural or forestry exploitations.	Taxable in the country where the exploitation is situated.	Taxable in the country in which the exploitation is situated.
2. Income from an industrial exploitation.	Taxable in the country in which the establishment is situated.	Taxable in the country in which the establishment is situated.
3. Income from the lease and rent of real estate or rights assimilable to the possession of real estate and tangible personal property.	Taxable in the country where the leased or rented property is situated.	Taxable in the country where the leased or rented property is situated.
4. Income from an independent business.	Taxable in the country where the business has its centre.	Taxable in the country where the business activities are permanently exercised.
5. Income (dividends) from a limited liability company.	Taxable in the country to which the company distributing the dividends belongs.	No exemption.
6. Income from mortgage.	No exemption.	Taxable in the country in which the mortgaged property is situated.
7. Income from sleeping-partners' shares in a partnership.	Taxable in the country where is situated the enterprise to which the capital is contributed.	No exemption.
8. Percentages paid to members of the Board of Directors of a share company.	No exemption.	Taxable in the country where the distributing company has its head office.
9. Income from speculation in real estate or in rights assimilable to the possession of real estate.	Taxable in the country where the real estate or rights are situated.	Taxable in the country where the estate or rights are situated.
10. Income from recurrent payments out of public funds.	Taxable in the country where the public funds are situated.	Taxable in the country where the public funds are situated.

PART III. — METHODS OF ALLOCATING TAXABLE INCOME.

A. FOREIGN ENTERPRISES WITH LOCAL BRANCHES OR SUBSIDIARIES.

I. GENERAL QUESTIONS AND METHODS OF APPORTIONMENT.

When an enterprise carrying on business in more than one country has in Danzig only a branch which keeps separate accounts, the authorities assess its taxable profits on the basis of the separate balance-sheet of the branch. If, on the contrary, the accounts of the entire enterprise are kept only at the foreign head office, the authorities divide the total on an apportionment basis.

(a) BOOK-KEEPING AND ACCOUNTING REQUIREMENTS.

In this connection, the requirements contained in paragraphs 156 to 159 of the Organic Tax Law of June 22nd, 1932 (*Law Bulletin*, page 497), are applied. The principal provisions contained in these paragraphs are the following :

“Enterprises which, when the tax was last assessed, had realised a turnover exceeding 200,000 florins, or had owned a business capital in excess of 50,000 florins, or agricultural property in excess of 100,000 florins, must keep accounts and regularly draw up balance-sheets. The taxpayers must, in particular, indicate the amount of their turnover. The books should be kept in accordance with a series of special provisions which, in fact, reproduce the general commercial usages collected in the Commercial Code under the heading ‘Principles of Regular Accountancy’. It is to be noted that the keeping of accounts of the passing of entries under a false or fictitious name, either on one’s own behalf or on the behalf of others, is forbidden. This prohibition applies also to a business enterprise owned by the taxpayer himself.”

(b) METHODS OF ALLOCATION.

I. *Method of Separate Accounting.*

In accordance with what has been said above, where there exists separate accounts for the Danzig branch, the authorities assess the income on the basis of the profits as shown in the accounts, corrected, if necessary, in accordance with the special provisions of the fiscal law. In checking the return, the authorities may ask for further information and may require the submission of balance-sheets. If the written information does not clearly show the taxable profits, they may proceed to a verification of the accounts.

The figures in the accounts of the branch which refer to relations with the foreign head office, such as charges representing a part of the general expenses of the enterprise, invoices for goods shipped or delivered to it, as well as interest on advances, are the subject of special scrutiny, in order to ascertain whether they conceal an unjustified transfer of profits in favour of the foreign part of the enterprise.

Further, the Danzig branch is obliged to give the fullest information as to the necessary data, and, if it should not conform with this obligation, particularly if it does not furnish the authorities with the information requested in connection with the head office accounts, the administration is entitled to estimate the taxable profits in an arbitrary manner.

Where, in the case of a branch or subsidiary of an enterprise having its head office or parent company in Poland or in the German Reich, it is necessary to verify the data given in the books relating to the accounts between the branch or subsidiary and the head office or parent company, the verification is made in accordance with the rules for fiscal assistance contained in the agreement with those countries. Incidentally, it may be noted that there are few branches belonging to enterprises with their head offices in countries other than Germany or Poland, and that their number is every day decreasing.

2. *Empirical Methods.*

If it is impossible to compute the profits on the basis of the separate accounts of the branch, or if no separate accounts exist, recourse may be had to the following alternative methods of assessment :

(a) The authorities may take into account the profits which would be realised by an independent Danzig enterprise of an identical or similar nature to that of the Danzig establishment, the taxable minimum being the normal rate of interest on the capital employed in the Danzig branch. For this purpose, the term capital is defined to mean, not only invested capital, but also working capital and, in particular, goods, products and equipment of the Danzig establishment. This method may be employed even if, in accordance with measures taken by the management of the business, the profits are apportioned in a different manner between the Danzig branch and the foreign head office.

(b) Income tax and company tax may be fixed at an arbitrary figure computed in an estimative manner in accordance with a "fiscal agreement". In the majority of cases, agreements of this kind are concluded for a number of years.

It may happen that, in certain cases, recourse is had to the methods indicated under (a) and (b) above, although it would be possible to determine the taxable income in a different manner. When it is necessary to make an estimative assessment, the authorities base it on the profits earned by an enterprise of a similar or identical nature, taking into account, at the same time, the importance of the enterprise. In order to form an opinion as to its measure of importance, the administration considers the following points : in the case of new enterprises, the rental value of the business premises, the amount of working capital and the number of employees ; in the case of enterprises already in existence, the administration considers, in addition to the above, the amount of turnover and of gross receipts during the past year. Fiscal agreements of this kind have been rather frequent, but they are concluded nearly exclusively with new enterprises. For some time past the fiscal authorities have adopted the rule that, when such agreements are entered into, the tax should not be fixed at an arbitrary figure but should have the nature of instalments representing a certain percentage of the tax normally assessable.

3. *Method of Fractional Apportionment.*

Finally, the authorities may assess the Danzig income as a fraction of the total net income, this fraction being determined on the basis of factors which, in view of the special circumstances of the enterprise, appear to be most appropriate for the determination of the profits earned. There are no special provisions governing the choice of the factors to be used for the apportionment of the

profit. In general, the authorities employ the following factors — for banks, etc. : amount of salaries and wages or gross receipts ; for insurance companies : premiums received ; for railways, buses and other transport enterprises : mileage ; for power, light and gas companies : the number of kilowatts or cubic metres furnished ; for telegraph and telephone companies : turnover ; for all other enterprises : salaries and wages paid. Where it is not possible to determine in a satisfactory manner the factors mentioned above, or where these factors do not furnish an appropriate basis for apportionment, the assessment authorities or the fiscal courts take into account the peculiar considerations of each case in determining the factors on the basis of which the profits attributable to the Free City should be computed.

4. *Requirements for Selection of Methods and Value of the Various Methods.*

It is within the competence of the assessment authorities or the fiscal courts to select which of the various methods should be employed. The decision must be inspired, not only by legal considerations, but also by considerations of justice. There is no empirical method which may be satisfactorily employed in every case. Each of the methods mentioned above may give adequate results according to the particular circumstances of the case. It is therefore impossible to indicate, among those enumerated above, any particular method which would be the most practical or satisfactory either because it is the most simple to apply or because it helps to prevent fiscal evasion.

(c) APPORTIONMENT BETWEEN BRANCH AND PARENT ENTERPRISE.

1. *Apportionment of Gross Profit of Local Branch to Real Centre of Management abroad.*

It is only in cases where the Danzig income is determined as a fraction of the total net income that this question becomes of importance. The fiscal law of the Free City does not authorise any set-off on this fraction in favour of the foreign head office, in view of the fact that in reciprocal cases it does not claim a similar right.

2. *Apportionment of Expenses of Real Centre of Management to Branch or Subsidiary.*

Interest Charges. — In this case, also, the solution depends on the methods of apportionment which have been selected. In general, account is taken of the peculiar nature of the debt. The burden of the interest charge is allocated to the part of the income to which the debt is economically connected. If, on the contrary, the debt is not economically connected to any special part of the income, the burden of the interest charge is apportioned between the countries concerned, in accordance with the same method as that which has been applied to the income.

General Overhead. — The same considerations as those given above apply here.

3. *Apportionment of Net Profit of Branch to Deficitary Parent and vice versa.*

Where the Danzig income is computed on the basis of the separate accounts or on the basis of the profits of similar enterprises (see above), no account should be taken of the final loss shown in the accounts of the entire enterprise. Even where the tax is assessed in an arbitrary manner, in accordance with a fiscal agreement (see above), no account is, as a rule, taken of the loss. On the other hand, such loss will be taken into consideration if the Danzig income is determined as a fraction of the total income of the enterprise.

Where the Danzig income is determined on the basis of its separate accounts, the loss shown by the Danzig establishment is taken into consideration in the course of assessment. On the other hand, in the case of a fiscal agreement, according to which the tax has been fixed at an arbitrary figure for a number of years, the loss is not usually taken into account. Finally, regard is never had to such a loss if the assessment is made on the basis of a comparison with the profits earned by Danzig enterprises of a similar nature or on the basis of fractional apportionment.

(d) APPORTIONMENT BETWEEN PARENT ENTERPRISES AND SUBSIDIARY.

Under the Danzig fiscal law, the local subsidiary of a foreign enterprise is subject to an unlimited tax-liability in the same way as any other independent taxpayer. The data of the balance-sheet of the parent company are never, therefore, taken into account when assessing the subsidiary in the Free City.

If the books of the subsidiary do not appear to reflect in a trustworthy manner the results of its transactions with the parent, the authorities may alter the balance-sheet of the subsidiary when, in accordance with international agreements in fiscal matters, they have the right to inspect the parent company's accounts, and when the results of this inspection justify such change. Finally, recourse may be had in such cases to empirical methods or to fractional apportionment, if this procedure appears more appropriate in the particular case.

II. APPLICATION OF THE METHODS OF ALLOCATION IN SPECIFIC CASES.

(a) INDUSTRIAL AND COMMERCIAL ENTERPRISES.

There is no special rule for assessing the profits taxable in respect of industrial and commercial enterprises. It should, however, be stated that such enterprises are taxable in Danzig if they possess in Danzig any of the following establishments: a *selling establishment* (whether selling in the Free City or abroad), a *manufacturing establishment* or a *processing establishment*, a purely *buying establishment*, *research establishments*, or other establishments not directly concerned in profit-making activities.

(b) OTHER ENTERPRISES.

No enterprise, whatever its nature, is subject to a special system of taxation. The method of assessment most frequently employed is that of assessing the tax on the basis of the separate accounts, which exist in the majority of cases. When the revenue authorities depart from this method and indicate one of the subsidiary methods (see page 145), their decisions are based on special considerations relating to the particular circumstances of the enterprise concerned, and not to the general class to which it belongs.

It cannot therefore be said, in regard to any of the various classes of enterprise, that any one method is more frequently used than others. These remarks are entirely general, and apply both to industrial enterprises and to other concerns.

B. NATIONAL ENTERPRISES WITH BRANCHES ABROAD.

In Danzig, national enterprises are taxable on the whole of their income — *i.e.*, including profits made abroad. There is therefore no need to allocate or apportion the income derived from different countries. Where, however, under double-taxation agreements concluded by the Free City, the

foreign State is entitled to tax the income received by one of the establishments abroad, allocation is effected by the judicious application of one of the methods examined above.

C. HOLDING COMPANIES.

Holding companies of Danzig nationality are exempt from company tax, but not from property tax. There are no special provisions relating to foreign holding companies having shares in Danzig companies, and, consequently, such companies are treated for fiscal purposes like any other person domiciled abroad and holding negotiable securities issued by Danzig companies.

Annex.

TABLE OF TARIFFS.

I. INCOME TAX.

(a) Rate applicable to Salaries and Wages.

Normal rate ¹ : 11 per cent of the taxable amount.

Minimum rate :

	Florins
Salaries and wages exceeding 100 florins per month	1.45
Salaries and wages exceeding 24 florins per week	0.35
Salaries and wages exceeding 4 florins per week	0.05

(b) Rate applicable to Directors' Percentages.

	Per cent
Percentages not exceeding 3,000 florins per year	10
Percentages exceeding 3,000 florins but not exceeding 10,000 florins per year	20
Percentages exceeding 10,000 florins per year	30

(c) Rate applicable to Other Income.

Normal rate :

	Per cent	
On the first 10,000 florins	11	
On the slice of income included between	10,000 and 15,000 florins	13.75
	15,000 and 20,000 florins	16.50
	20,000 and 30,000 florins	22
	30,000 and 40,000 florins	27.50
40,000 and 80,000 florins	33	
On all further amounts	38.50	

Minimum rate ² : 17.60 florins.

¹ The taxable amount consists of the actual amount of the salaries and wages minus the amounts deducted as professional expenditure and allowances for dependents as indicated on page 133.

² For taxpayers whose net income, excluding the allowances for dependents and tax-free minimum, exceeds 600 florins per year.

(d) *Emergency Surtax.*I. *On Income from Labour.*

Per cent

Taxpayers liable to the tax on fixed salaries ¹. 1½

For other employees :

Amount received monthly	RATE OF SURTAX	
	Unmarried persons, married persons without children, married persons with one minor child	Individuals having more than one minor child
Florins	Per cent	Per cent
Up to 100	—	—
From 101 up to 150	2.0	1.75
From 151 up to 200	2.5	2.00
From 201 up to 400	3.5	2.50
From 401 up to 800	4.5	3.00
From 801 up to 1,600	5.5	5.50
In excess of 1,600	6.5	6.50

2. *On Other Income.*

Amount of the yearly income or of the fraction of the taxpayer's property taken as a basis for the computation of the tax in accordance with paragraph 5 of the Ordinance of September 26th, 1931	RATE OF SURTAX	
	Unmarried persons, married persons without children, married persons with one minor child ²	Taxpayers with more than one minor child
Florins	Per cent	Per cent
Up to 600	—	—
From 601 up to 1,500	$\frac{3}{4}$	0.375
From 1,501 up to 2,500	1½	$\frac{3}{4}$
From 2,501 up to 5,000	3	1½
From 5,001 up to 10,000	4½	2¼
In excess of 10,000	6	6

II. COMPANY TAX.³

Per cent

Profit-seeking corporations 20

Other companies and legal entities 10

¹ See definition, page 128.

² The rate below is also applicable to the taxpayers subject to company tax.

³ The scale of the emergency surtax on companies is the same as that which is contained in the first two columns of the last table above.

III. BUSINESS TAX.

Minimum Tax.

Classes of taxpayers	Annual amount of the tax Florins
First	2,400
Second	1,200
Third	480
Fourth	240
Fifth	120
Sixth	40
Seventh	Nil

Normal Tax.

Slices of the taxable profit comprised between and (in florins)	Percentage of tax applicable to each slice
0 2,400	Nil
2,400 4,800	3
4,800 7,200	6
7,200 9,600	9
9,600 12,000	10
12,000 16,800	11
In excess of 16,800	12

IV. PROPERTY TAX.

Amount of the property (in florins)	Percentage of tax applicable to the total amount of the taxable property
Not exceeding 10,000	Nil
Between 10,000 and 12,500	2
Between 12,500 and 30,000	3
Between 30,000 and 60,000	4
In excess of 60,000	5

GREECE

BY

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PART I. — GENERAL DESCRIPTION OF DIRECT TAXATION SYSTEM¹

The existing income-tax system was introduced in Greece in the main at the time of the tax reforms of 1919, and its study necessitates a short account of the original fiscal system.

There were formerly seven schedular taxes, each assessed upon the net sum of a given category of income. These taxes were :

- Category A : Tax on income from buildings.
- Category B : Tax on income from leased land.
- Category C : Tax on income from securities.
- Category D : Tax on income from profits of commercial and industrial enterprises.
- Category E : Tax on income from agriculture.
- Category F : Tax on salaries and wages.
- Category G : Tax on remuneration from the liberal professions.

As regards agricultural enterprises, there were also a few ancient taxes on gross income, but these, although not abolished by the reform, were supplanted later.

The scale of the schedular taxes and of taxes on gross agricultural output was, in principle, proportional, except for certain basic relief in the case of income of Categories D, E, F and G.

In addition to these taxes, there was the complementary tax on the total income of individuals — a graduated tax.

However, the political and economic difficulties by which Greece was beset subsequently to the reforms led to many alterations of the original fiscal system.

While the taxes on income from leased land and buildings have undergone amendments of detail hardly worth mentioning, the alterations in the taxes on industrial and commercial profits, remuneration from liberal professions, and agricultural profits are of quite a different character. The introduction of a tax assessed exclusively upon the net income of commercial and industrial enterprises caused such difficulties, both to taxpayers and to the Administration, that it was found necessary to revert to the former procedure and, in part, to replace the schedular tax by a *patente* tax, computed sometimes on the basis of a presumed average income, sometimes in the special way described below.

The same was true of the liberal professions, with the result that, as regards both these classes of income, two taxes are imposed — the *patente* tax and the tax on the net income.

The changes were still more drastic in the case of agricultural enterprises. In the place of a single schedular tax computed on the net income of all farmers alike, there is now one tax on the net income from certain stock-breeding enterprises, and there are four taxes assessed either on gross income or by an empirical method.

Accordingly, the system of direct taxes in Greece is now as follows :²

Buildings : a tax on net income (Category A).

¹ Legislation in force on May 15th, 1933.

² The following figures, taken from the accounts for the financial year 1930-31, show, in millions of drachmas, the relation between direct taxes and other fiscal revenue of the Republic : direct taxes, 1,379.3 ; taxes on legacies, bequests, etc., 140.3 ; Customs, 2,709.1 ; consumption taxes, 1,603.2 ; monopolies, 230 ; stamp duties, 590 ; other Government duties, 171.9 ; miscellaneous revenue, 71.8 ; additional tax for the service of the national debt, 1,329.6 ; extraordinary revenue, 251.2 ; revenue brought forward from previous years, 111.6 ; total, 8,588.

Leased land : a tax on net income (Category B).

Securities : a tax on net income (Category C).

Industrial and commercial enterprises : (1) a *patente* tax ; (2) a tax on net income (Category D).

Agricultural enterprises : (1) a tax on net income (Category E) ; (2) various taxes computed on gross income or empirically.

Salaries and wages : a tax on the income (Category F).

Liberal professions : (1) a *patente* tax ; (2) a tax on net income (Category G).

Total income : a complementary tax on the total net income of individuals liable to tax in Greece.

I. TAXPAYERS.

(a) INDIVIDUALS.

Persons domiciled or resident in Greece.

The law relating to direct taxes contains no definition of domicile, and the term is understood in the sense it bears in civil law.

Persons who have resided in the country for more than six months of the year preceding the tax year are assimilated in all respects to persons domiciled there.

Persons, however, who, although domiciled in Greece, have resided abroad for the two years preceding the tax year do not incur the obligations of a taxpayer domiciled in Greece. The law also says that a married woman, for purposes of the tax on total income, has not necessarily the same domicile as her husband, but is only liable to the tax when the requisite conditions of domicile and residence apply to her own person. Consequently, a married woman whose husband enjoys exemption on the score of two years' absence is not herself exempt unless her own position satisfies the conditions of the clause, and, if she is resident at the family domicile in Greece, she will be personally liable to tax. The converse also holds good.

Persons domiciled in Greece or resident there for six months are, in principle, liable to all the schedular taxes, if they derive income from the country.

On the same grounds, individuals are liable (a) to the schedular taxes on securities and on remuneration from salaried work and the liberal professions, in respect of income of these classes they derive from abroad ; and (b) to the tax on total net personal income leviable against these same classes of income.

Independently of domicile or length of residence in Greece, individuals are also liable to the schedular taxes on industrial and commercial enterprises in respect of profits they derive from abroad, in the cases more particularly dealt with on page 163.

Nevertheless, any tax or impost paid abroad on income from commercial and industrial enterprises, salaried services or the liberal professions is deducted from the tax levied in Greece on the net income of Categories D, F and G.

Persons domiciled abroad.

This term only includes persons who have not resided in Greece for more than six months, since, as already explained, persons resident for a longer period are assimilated to taxpayers domiciled in the country. Further, officials serving abroad are in all cases regarded as domiciled in Greece.

Persons domiciled abroad are only liable to the schedular or analytical taxes if they derive income from a Greek source. They are never liable to the tax on total income, even in respect of income earned in Greece.

Taxpayers of Foreign Nationality.

Fiscal liability is conditioned by the domicile or residence of the taxpayer, and questions of nationality play, as a rule, no part. According to a recent law, however, foreigners established in Greece are granted exemption — subject to reciprocity — from schedular taxes and the tax on total income in respect of income of any kind derived from abroad.

(b) PARTNERSHIPS.

In Greece, this term comprises general partnerships (*sociétés en nom collectif*) and limited partnerships (*sociétés en commandite simple*).

The schedular and *patente* taxes imposed upon individuals are leviable also against partnerships, either as such or against the members, as explained below. Partnerships are not liable to the tax on total income, but their members have to pay it on their share of profits if the conditions of their domicile or residence in Greece are such as to justify taxation.

As regards the extent of fiscal liability, what was said above concerning individuals applies also to partnerships. That is, partnerships established in Greece are treated in the same way as individuals domiciled there, and partnerships domiciled abroad are on the same footing as private persons with a foreign domicile.

*(c) COMPANIES.**National.*

National share companies are by their nature liable to the *patente* tax, which is small (see page 167) and to class (a) of Category C tax on the profits they distribute (see page 160). Under certain conditions (see page 161), they may be made liable to Category D tax on their total profits instead of to Category C tax.

They are further liable, in respect of their real property, to the taxes on income from buildings and leased land. They also pay securities tax on interest, dividends and other capital yield accruing to them from third parties. There are, however, certain exemptions in their favour to which reference will be made later (see page 161).

Foreign.

Foreign share companies are liable to the *patente* tax. As will shortly be shown, this tax is determined in their case otherwise than for national companies; but again the tax is small.

They are further subject, not to Category C tax, like national companies, but to Category D tax — *i.e.*, tax on the income of commercial enterprises.

Since the dividends of foreign companies are mostly distributed and paid abroad, those companies would not, in practice, have paid tax on their Greek profits if the tax on securities had been levied against them.

Foreign companies may, however, at their request and with the consent of the Ministry of Finance, pay the tax on securities (class (a) of Category C) instead of tax on the income of industrial and commercial enterprises (Category D). But, once this arrangement has been made, it must hold good for three years. This right to be assimilated to national companies is of particular importance to enterprises which are earning a profit in Greece while incurring expenses or losses abroad.

Foreign share companies are liable, just like national companies of the same kind, to taxes on income from leased land and buildings in respect of their real property in Greece and to the tax on securities if they receive capital income in Greece.

2. TAXABLE INCOME.

INCOME FROM BUILDINGS.

The net income from buildings situated in Greece (determined as explained under No. 3 below) is liable to Category A tax. It does not matter whether the recipient of the income is domiciled (or resident) in Greece or abroad. On the other hand, the income from property situated abroad is not taxed, even if the property belongs to persons or legal entities domiciled in Greece.

Exemptions. — The following are exempt from this tax : property belonging to the State, municipalities and communes ; churches ; buildings belonging to educational or charitable institutions and not used for lucrative purposes ; premises belonging to foreign legations (subject to reciprocity) ; factories, if not let ; premises owned by hotel companies ; houses inhabited by the owner and the annual income from which does not exceed 3,000 drachmas ; farm buildings and certain classes of small houses.

Owing to the housing crisis induced by the influx of refugees, buildings erected between 1923 and July 1926 are tax-free for periods varying between four and twenty-five years.

INCOME FROM LEASED LAND.

The tax on leased land, like the tax on buildings, is assessed upon net income and is imposed on income from the letting of land and agricultural estate situated in Greece, irrespective of the domicile or residence of the recipient of the income. Income from property of this kind situated abroad is never taxed. Nor is the tax levied, even on the basis of rental value, when land is not leased, but is cultivated by the owner. In such cases only the tax on agricultural development is collected, as explained below.

Exemptions. — Mines and quarries are not liable to this tax, but are subject to a special regime (see page 169). Further, land belonging to the State, municipalities or communes and to religious establishments is exempt.

INCOME FROM SECURITIES.

This form of income is classified under Category C, which has three subdivisions, and tax is imposed upon any individual or legal entity enjoying income from one or other of the classes enumerated below.

Class (a).

Class (a) includes income from securities issued by legal entities and companies of Hellenic nationality. The law, however, provides for many exemptions and, in practice, only the following income of this class is taxed.

- (1) Dividends from shares in Hellenic share companies ;¹
- (2) The remuneration and percentages paid to the members of the boards of these companies ;
- (3) The remuneration or percentages paid to the directors and managers of these companies over and above their salaries ;

¹ In the event of the company's dissolution, any sums paid to shareholders over and above the paid-up capital are regarded as a distribution of dividends and, as such, taxable.

(4) The portion of the salaries of the staff of these companies which exceeds twice the amount fixed as the tax-free minimum for purposes of tax on total income ;¹

(5) Interest of any kind on the bonds of companies, co-operatives and legal entities of Hellenic nationality.

These forms of income are taxable irrespective of the recipients' domicile or residence, with the result that Greek securities held abroad are not, in principle, tax-free (but see under "Exemptions" below).

The class is, in fact, made up mainly of income distributed by national companies, since Government securities and interest on debts of public corporations are free of tax, while the securities issued by other legal entities are few in number.

As regards share companies, a recent law prescribes that companies incorporated subsequently to April 1st, 1926, and which distribute dividends amounting to less than 5 per cent of their paid-up capital, may pay Category D tax on their total profits. For this purpose, however, there must be a ministerial decision given on the recommendation of a special committee made up of officials and of representatives of the Union of Share Companies. Should this tax on total profits be applied, dividends, directors' percentages, etc., distributed by the company are not liable to the tax on class (a). Another provision deals with holding companies, and, with a view to avoiding their double taxation, provides for the issue of a decree conditionally reducing the tax payable on the dividends, etc., of a holding company, when it redistributes the dividends of a national company on which class (a) tax has already been paid.²

Exemptions. — The following income is exempt from this tax :

- (1) Interest on public loans ;
- (2) Interest on loans contracted by municipalities, communes and ports ;
- (3) Interest on bonds issued by Hellenic industrial share companies ;
- (4) Interest on loans granted to Hellenic share companies by foreigners or by nationals permanently settled abroad ;
- (5) The profits distributed by national lignite-extracting enterprises and the interest on their loans.

In cases (3) and (4), interest is not tax-free if it was deducted from the taxable income from real estate belonging to the debtor company.

Class (b).

Class (b) consists of income from foreign securities ; it is taxable (1) whatever the recipients' domicile or residence, when paid or received through a bank, in Greece ;³ (2) when the income, although paid abroad, accrues to persons who are domiciled in Greece or have resided there for at least six months.

Exemptions. — Subject to reciprocity, (1) the income of foreign diplomatic and consular agents

¹ These salaries, are, however, held liable to Category F tax.

² No decree of this kind has yet been issued.

³ The Administration has issued instructions that this income also shall only be taxed if the recipient is domiciled in Greece or has resided there for six months.

and (2) the income of any foreigner, even if he has resided in Greece for more than six months, are exempt from this tax.¹

Class (c).

Class (c) comprises interest of whatever origin not included in classes (a) and (b) — *i.e.*, interest on any unsecured, mortgage or other debt and on all deposits, sureties, etc. The interest in this class is divided into : (1) interest of Greek origin on which tax is levied without regard to the domicile or residence of the beneficiary ; (2) interest from foreign sources ; in this case the recipient is only liable to tax if he has a domicile or has resided in Greece for at least six months.

Exemptions. — The following income is tax-free :

- (1) Interest on deposits of all kinds with national banking institutions ;
- (2) Interest on credits and remittances of Hellenic banks from abroad ; the interest thus exempted must not exceed the official rate of discount of the country whence the capital originates, but in the case of institutions whose sole purpose is to grant loans on tobacco, the exempted rate may not fall below 5 per cent ;
- (3) Interest on deposits with public savings banks ;
- (4) Interest on loans granted by foreigners or by nationals settled permanently abroad granted to national enterprises of some importance ; exemption is refused if the interest was deducted from the taxable income of buildings belonging to the debtor enterprise ; interest on loans, with a mortgage-guarantee on Greek ships, granted by foreigners abroad are likewise exempted ;
- (5) Interest on foreign credits granted for the import of goods or export of the products of agriculture and stock-breeding, either in the raw state or after treatment ; the real purpose of these credits must be duly established ;
- (6) Income accruing to Hellenic share companies from interest of this class ;
- (7) The income of foreign diplomatic and consular agents, subject to reciprocity ;²
- (8) Income of this class accruing to any enterprise which operates lignite mines in Greece ;
- (9) Subject to reciprocity, income derived from foreign sources by foreigners, even if they have resided in Greece for more than six months.³

The following income, although similar to that of the present class, is exempt from the tax imposed on the latter, and is liable to Category D tax :

- (1) Interest on drafts and bills of exchange pertaining to commercial transactions, and
- (2) Interest earned by banks not constituted in the form of a national share company.

PROFITS OF INDUSTRIAL AND COMMERCIAL ENTERPRISES.

The profits of industrial and commercial enterprises (other than share companies of Hellenic nationality) which do business in Greece are, in principle, liable to the *patente* tax and to Category D tax on net income.

¹ The first case applies generally, but not the second, no convention with other countries having yet been concluded.

² This exemption is general.

³ This exemption is not yet in force, as no convention on the subject has yet been signed with other countries.

The fiscal treatment of this form of income has undergone frequent changes since the tax reforms of 1919, mainly on account of the serious inconveniences which the sudden imposition of a tax on net income caused both to the Administration and to taxpayers who were accustomed to pay nothing more than a simple *patente* tax. Accordingly, the original form of the tax, which was purely a tax on net income, has been amended in several respects. Under the present system, the profits of industrial and commercial enterprises are liable to a *patente* tax plus, in some cases, a tax on net income. Further, as will be seen from No. 3 below, the fiscal treatment of shipping, tobacco and mining enterprises and of foreign share companies differs in many points from the normal regime applying to industry and commerce. The taxable income, as will be explained in detail under No. 3, is sometimes the net profit actually earned, sometimes an assumed net profit.

In every case profits are taxable if their source is national, whatever the domicile or residence of the taxpayer or the head office of the taxable enterprise.

The profits of foreign vessels calling at Greek ports are liable to Category D tax if they accrue to a share company (page 169) or to the general *patente* tax (page 166) plus Category D tax in other cases ; exemption from all these taxes may be granted on a basis of reciprocity.¹

Certain profits, however, which may be regarded as of foreign origin are also liable. This assimilation to purely Greek income takes place :

(a) In the case of profits from Greek shipping. As we shall see hereafter, Greek vessels are in all cases subject to the *patente* tax and there is at present no provision which allows any account to be taken of taxes paid abroad. However, the reciprocal exemption of national and foreign vessels is possible under the conditions just mentioned.

(b) In the case of profits from business transacted abroad by Category D taxpayers through branches, agents or representatives dependent upon an enterprise whose centre or seat of management is in Greece. Tax paid abroad in respect of these profits is deducted from the tax due in Greece up to the amount of the latter. As regards foreign enterprises, branches or subsidiaries situated outside the country are only taxed when they depend upon the office of the company in Greece, and in this case, not only may any tax paid abroad on foreign profits be deducted, but, subject to reciprocity, these foreign profits are totally exempt.

The above rules do not apply to tobacco enterprises, either national or foreign, which are governed exclusively by the provisions explained below under the heading " Assessment of Tax ".

With regard to tax-free industrial and commercial profits, see also the heading " Assessment of Tax " accompanying the chapter on each tax.

PROFITS FROM AGRICULTURE.

The fiscal treatment of profits from agricultural enterprises has undergone several modifications since the reforms of 1919. The present system of taxation cannot be regarded as final and a new method is now under consideration. This class of income is liable, according to its nature, to one of the following taxes :

- (a) the tobacco tax ;
- (b) the oil tax ;
- (c) the tax on raisins and currants ;
- (d) the tax on other agricultural products ;
- (e) the tax on stock-breeding.

The first four of these taxes are assessed either on gross income or empirically. The tax on stock-breeding, when enforced, is a tax on net income (Category E).

The rules governing the assessment and collection of these taxes will be studied in due course.

¹ Conventions granting mutual exemptions have been signed with France, the United States of America, the United Kingdom, Canada, the Netherlands, Norway, Sweden and Italy ; negotiations are proceeding with Belgium and Yugoslavia.

SALARIES AND WAGES.

Category F tax is levied, in principle, upon wages, salaries and retiring pensions of Greek origin. Income of this class is also taxed when it is of foreign origin, if the recipient is domiciled in Greece or has resided there for at least six months. In this case, however, the tax paid abroad on this income is always deducted from the amount payable in Greece. Further, income of this kind derived from abroad by foreigners settled in Greece may be exempt from the tax on a basis of reciprocity.

INCOME FROM THE LIBERAL PROFESSIONS.

Remuneration from the liberal professions is liable to tax if it is in return for services rendered in Greece. The taxes levied are the *patente* tax and the tax on Category G income.

Income, however, of this class received abroad by persons liable to Category G tax and domiciled in Greece or resident there for more than six months is also taxable. The provisions concerning the abatements and exemptions granted to national or foreign taxpayers by reason of the origin of the income are the same as those applying to salaries and wages.

COMPLEMENTARY TAX ON TOTAL NET INCOME.

This tax is levied only upon individuals who are domiciled in Greece or have resided there for six months. The taxable income is the total income already liable to one of the other taxes. It also includes income earned abroad or in Greece and not already taxed in Greece.

3. ASSESSMENT OF TAX.

TAXATION OF INCOME FROM BUILDINGS.

Category A tax on income from buildings is assessed, not annually, but for a number of years fixed by decree. On the occasion of each assessment, taxpayers have to make a declaration, which, after being checked by the Administration, serves as the basis of taxation for the ensuing years. But if there is an increase or diminution in income of more than 10 per cent, the tax list is altered accordingly.

The taxable income is determined on the basis of the net income actually received during the year preceding the tax year. If, however, there is a substantial difference between the actual income and the rental value, or if the premises are not let, the law prescribes that tax shall be based on rental value.

To get the net income, the following deductions are made from gross income : (a) 10 per cent for depreciation and cost of upkeep ; (b) interest on secured loans ; (c) local taxes, and (d) a few other minor deductions.

The tax is proportional and there is no tax-free minimum.

TAXATION OF INCOME FROM LEASED LAND.

Unlike the previous tax, Category B tax on income from leased land is assessed annually, and taxpayers have to declare their income in April of each year.

The taxable income consists of the income actually earned in the fiscal or business year preceding the tax year. Actual income is obtained by deducting from the rent : (a) 5 per cent for depreciation and maintenance ; (b) special depreciation for drainage work, etc. ; (c) interest on mortgage loans,

and (d) local taxes. If there is any difficulty in determining the gross income, the rules governing Category A apply *mutatis mutandis*.

This tax, like the previous one, is proportional, and similarly there is no tax-free minimum.

TAXATION OF INCOME FROM SECURITIES.

The income of all three classes (a), (b), and (c) is taxed after deduction of all taxes and imposts already levied. There is, however, no tax-free minimum and the rate is proportional.

The three classes call for the following observations :

Class (a).

The tax on income distributed by Hellenic share companies is levied upon shareholders and others who participate in the company's profits, but payment is actually made to the Treasury by the company, which can withhold the tax from the dividends, directors' percentages, etc., it distributes. The tax is paid in a single instalment within two months of the approval of the balance-sheet by the general meeting of shareholders. A declaration in support of the sum paid is forwarded at the same time. The tax on other income of this class is similarly paid by deduction at source, the declaration being submitted and the tax paid within a month of the date fixed for the payment of coupons.

Class (b).

The office in Greece which collects or pays this class of income from foreign sources has to withhold tax and to pay the whole amount to the Treasury in the course of the following April, accompanying its payment by a supporting statement.

Anyone who directly receives income abroad must declare it during April of the year following receipt, and pay the tax to the Treasury in a single instalment.

Class (c).

As regards income from Greek sources, the tax is paid by affixing stamps to the document establishing payment. In the case, however, of income from abroad received either directly or through an establishment in Greece, the person concerned must make a declaration and pay the tax to the Treasury in April of the year following receipt of the income.

TAXATION OF THE PROFITS FROM INDUSTRIAL AND COMMERCIAL ENTERPRISES.

As explained on pages 162 and 163 the taxation of these enterprises now includes : (a) *patente* tax and (b) Category D tax on net income. Let us examine these two taxes in detail.

There is, further, a separate regime for mines.

(a) *Patente Tax on Industrial and Commercial Enterprises.*

The rules for the assessment of *patente* tax are not the same for companies as for other taxpayers. Moreover, shipping and tobacco enterprises receive special treatment. We shall therefore deal successively with the four following points :

- Rules applying to ordinary taxpayers ;
- Special rules for national and foreign share companies ;
- Special rules applying to tobacco enterprises ;
- Special rules applying to shipping concerns.

(1) *General Patente Tax.*

In the case of taxpayers who are not share companies or are not concerned with either shipping or tobacco business, the *patente* tax is assessed on their probable or assumed net income. For purposes of this tax, the law divides taxpayers into thirty groups according to the size of their incomes, and a certain tax figure is fixed for each group. The lowest group includes taxpayers whose assumed income does not exceed 25,000 drachmas, and for these the *patente* tax is fixed at 600 drachmas. The highest group is made up of persons with an income of 300,000 drachmas or more; in their case, the tax is 39,000 drachmas.

In small towns and villages, the tax may in exceptional cases be reduced for the lowest group of taxpayer to 50 drachmas.

The assumed annual income which puts taxpayers into one of the thirty groups is ascertained by taking the taxpayer's average profits for the three years preceding the establishment of the tax-lists; in practice, that is, the three years since their last fiscal classification.

The tax is payable by (a) anyone who conducts an enterprise in person; (b) each of the partners in a partnership; (c) limited partnerships, co-operatives, etc.

These provisions apply indiscriminately to private persons and legal entities, both national and foreign.

Foreign commercial travellers, agents and representatives are liable to this tax on any business they do in Greece.

Enterprises with several branches or agencies in Greece are taxed at their head office on their total profits; each office or agency has further to pay the *patente* tax of the lowest group.

The tax is not payable by:

- (a) Co-operatives which supply their members only;
- (b) Owners of foreign vessels, subject to reciprocity (for details, see page 163);
- (c) Enterprises of any kind which work lignite mines in Greece;
- (d) Certain classes of small artisan or tradesman.

New enterprises are, for the first year of their existence, classified provisionally on the basis of their probable profits, final classification being made in the following year.

If a taxpayer goes out of business, his name is taken off the lists the next year. As regards the tax he owes for the year in which he ceased doing business, he is allowed relief proportioned to the difference between the income actually earned and the income of his group.

Tax is assessed and taxpayers are classified on the basis of a declaration which the taxpayer has to furnish to the Administration. The declarations are checked with the help of delegates appointed by the unions of the traders concerned.

The lists drawn up as the result of classification remain in force for three years, but under certain conditions the entries in the lists may be altered during this period if the taxpayer's income has increased or diminished.

The period of three years may, in exceptional cases, be extended or shortened by decree.

In order to determine the total tax, the presumed income is that corresponding to the group in which the taxpayer has been placed. He is, however, allowed to show proof that his actual income was less than the assumed figure, or even that he sustained a loss. The Administration, too, is at liberty to show that the real income exceeded the figure assumed.

Taxpayers liable to the present category of *patente* tax are also liable to Category D tax on net income, if the latter exceeds 300,000 drachmas (see page 169).

(2) *Special Patente Tax on Greek and Foreign Share Companies.*

The *patente* tax levied upon Greek share companies is fixed in relation to paid-up capital, the

rate being 2.5 per thousand thereof. By way of exception, shipping companies may choose to pay the special *patente* tax on shipping (see below).

The *patente* tax payable by foreign share companies (whatever their size) is 25,000 drachmas per annum. The tax could not be determined in the same way for them as for national companies, since it is difficult to say how much of their capital has been devoted to business done in Greece. Shipping companies are exempt, subject to reciprocity (see page 163).

In April of each year, national and foreign companies alike must submit a declaration to the Administration for purposes of *patente* tax.

(3) *Special Patente Tax on Greek Shipping Enterprises.*

The *patente* tax payable by ships flying the Greek flag is determined on the basis of tonnage. But, although thus computed, the tax is intended by the law to fall upon an assumed average profit for a number of years. In order that shipping may escape as lightly as possible, the rate is very low. Category D tax on net income is never imposed on Greek ships, whatever profits they may have earned.

Shipping companies may apply to be subjected to the special *patente* tax on shipping enterprises instead of to the tax on paid-up capital mentioned under (2) above.

Taxpayers liable to the present tax must make an annual declaration to the Treasury in April.

For purposes of the total tax levied upon the owner of the vessel, the income from its exploitation is assumed to be seven times the tax, after deducting interest on mortgage loans. The Treasury, however, as mentioned on page 166, may show that the net profit earned was larger, while the taxpayer may plead a smaller profit or a loss.

(4) *Special Patente Tax on Tobacco Enterprises.*

The taxation of tobacco enterprises is of particular importance from the point of view of double taxation, because a large share of the tobacco trade is in the hands of foreigners.

Tobacco is Greece's premier agricultural export, representing 55 to 60 per cent of the value of all Greek exports; the bulk of the tobacco grown is for export.

Before it is exported, tobacco is divided according to quality and undergoes certain processes with a view to improving that quality. Many merchants store tobacco in Greek warehouses until finally sold, and their operations start with the purchase of the tobacco direct from the grower. Owing to the commercial importance of these Greek operations, tobacco businesses are liable to tax in Greece, even though the final profit or loss is earned abroad.

History. — Before describing the fiscal regime of to-day, it may be well to cast a glance at earlier methods of taxation. Originally, the law prescribed that, when the profits on tobacco export were not apparent from the balance-sheets of the enterprises concerned, the profits taxable in Greece must be computed by one of the three following methods :

(a) On the basis of the ratio between the turnover of sales of exported tobacco and the turnover of all sales.

(b) By taking, as the gross profit, the f.o.b. wholesale price of exported tobacco, as quoted on the day of export (whether the tobacco was sold or not) and by comparing this gross figure with the cost of production plus general overhead, etc., of the branch. The result of this comparison was either an assumed net profit on which tax was assessed, or a loss.

(c) If the f.o.b. price could not be determined, the profit might be estimated at a certain percentage of the cost of production of the exported article, this percentage being fixed by a special committee.

Of these three methods, the first was found almost unworkable, owing to the difficulties which enterprises had in computing the profit earned in Greece ; moreover, tobacco was often sold abroad as cigarettes after being mixed with tobacco of other origin. The second method likewise encountered serious obstacles. In the first place, tobacco prices, in places where there was no exchange, were not always officially fixed ; and, secondly, firms could not tell exactly which of the tobaccos they had bought were exported, as the products supplied by the growers had been subjected to selection and other treatment before being exported. The third method was very easy to apply ; it was based on the view that the Greek branch of enterprises selling abroad was merely the representative or agent of these enterprises and was paid by a commission on operations effected in Greece.

The methods of computing profits referred to above applied, of course, only to foreign enterprises. In the case of Greek concerns, the whole of the profit earned abroad had to be declared.

With regard to the internal trade in tobacco, the factor to be considered was the actual net profit.

Taxable profit having been determined, the taxpayer was held liable to the tax applying to his particular form of enterprise : Category C tax, for Greek share companies ; Category D tax, for foreign share companies, and the *patente* tax plus Category D tax for other companies.

These provisions were in force until the end of the tax year 1930-31. As from 1931-32 all these taxes were abolished for tobacco enterprises and replaced by a special *patente* tax, the only distinction being between export trade and home trade.

Existing Regime. — Export trade : In the case of Greek or foreign enterprises which export tobacco leaf, the new *patente* tax is computed, as regards foreign sales, according to the number of oca¹ of tobacco exported.

Tax is fixed in relation to quantity, because the latter is carefully recorded in the books of the Treasury offices, which keep a close check on each enterprise in the interests of consumption tax and the tax on tobacco manufacture. The tax varies, according to locality of production, from 0.10 to 0.60 drachma per oca.

The area of production and amount of tax per oca in each are fixed by a special committee. The committee recently set up has fixed the tax scale on the basis of the average cost of production in each area, applying a certain percentage to this figure.

Accordingly, the system of taxation approximates to the third of the earlier methods described above, and the tax is levied on a presumed sum which the committee ascribes to the operations of the establishment in Greece.

The enterprises concerned have to declare in April of each year the amount of tobacco they exported during the preceding year.

Home trade : As the home market absorbs only a small part of the output, it has not been found necessary to establish a different regime from that governing export business. The tax is therefore fixed at a certain sum per oca of tobacco sold. But, as in home trade the same quantity of tobacco may be sold over and over again, the rate of tax is about half the rate pertaining to exports. Again, annual declarations are required.

For purposes of tax on total income, the latter is assumed to be equal to seven times the *patente* tax paid, the taxpayer and the Treasury being free to show that the actual income is less or more than the assumed figure (see page 166).

¹ An oca is equal to 1,282 grammes.

(b) *Category D Tax on Net Income.*

This tax does not apply to national shipping enterprises (see page 167) or to tobacco concerns (see page 168) in whatever form they are incorporated. Excluding these two forms of enterprise and the lower groups of *patente* taxpayers (see page 166), this tax is payable by :

- (1) Taxpayers liable to the general *patente* tax (page 166) whose net profits exceed 300,000 drachmæ ; the Category D tax payable on amounts exceeding 300,000 is thus a surtax ;
- (2) Foreign share companies, irrespective of their profits ;
- (3) In certain cases, national share companies incorporated after April 1st, 1926 (see page 161).

For purposes of the present tax, the enterprise's net income is regarded as the taxable figure. The following items are also included among taxable profits, but only up to four-fifths of their amount : (a) gain from the sale of a business, industry, etc. ; (b) profit from the sale of any intangible asset ; (c) appreciation of an enterprise's capital, except real estate.

The methods of determining taxable income, formerly in force for tobacco enterprises, but now amended in their case (see pages 167 and 168) are still employed for other enterprises whose purpose is the production, or simply the working-up, of raw materials.

Exemptions from this tax are as follows :

- (a) Subject to reciprocity, the profits earned in Greece by foreign vessels (see page 163) ;
- (b) Profits from the working of lignite mines in Greece ;
- (c) As regards foreign share companies whose shares are held wholly or partly in Greece, the proportion of the Greek profits corresponding to the number of nominal shares, the dividend on which is paid in Greece and is therefore liable to class (b) of Category C tax.

This class of taxpayer has to make a declaration of net income in April of each year. In the exercise of its right of control, the Administration may obtain assistance from advisory bodies similar to those employed for the assessment of *patente* tax.

(c) *Taxation of Mines.*

All mines are subject to a property tax fixed according to the area leased and known as the " area tax ". It is doubled if the mine is not worked.

The income from the working of mines and quarries is also liable to the tax on net income. If the mine is operated by a Greek company, Category C tax is paid ; otherwise, the *patente* tax or Category D tax on net income.

If the concessionaire of a mine does not work it personally, but leases it to a third party, he is liable to a special tax on the rent.

All these taxes on mines and quarries in Greece are imposed irrespective of the domicile, residence or head office of the person enjoying the income.

Lignite mines are exempt.

TAX ON AGRICULTURAL PROFITS.

The tobacco tax is assessed on the price which the grower obtains from sales to dealers and is paid direct to the State Treasury in cash. Every operation in tobacco, from the harvest until it is placed for consumption on the home market or exported abroad, is controlled by the Treasury simultaneously with its control over the tax on tobacco consumption.

The oil tax is assessed as follows :

(a) As regards oil produced in the Greek islands and in a few other districts, the tax is collected at the time of export from the isles to other parts of Greece or abroad and is computed on the basis of the export price ;

(b) As regards oil from other parts of the country, the tax is paid at the time of production and is computed according to output. It is either farmed out or collected by the Treasury direct. The producer may pay in cash or in kind.

The tax on raisins is paid in cash at the time of export. *The tax on currants* is paid to the Treasury by a special body, the Central Currants Office, the amount being fixed by decree at a flat rate according to the general conditions governing the production and export of the commodity.

The tax on other agricultural products, according to the fiscal reforms of 1919, was a tax on net income, but was later replaced by other contributions. There is now an allocated tax (*impôt de répartition*) on gross output ; this tax has, however, been provisionally suspended since 1930-31 as an encouragement to agriculture.

The tax on stock-breeding only affects profits from the breeding of big live-stock. It is a tax on net income of Category E, and the taxable sum is the net profit from stock-breeding after deducting 25,000 drachmas as tax-free.

TAX ON SALARIES AND WAGES.

This tax is assessed on the amount of taxable remuneration, but the recipients do not, as a rule, have to make a declaration, the tax being withheld at the source by the employer, who has to supply the necessary confirmation when paying the sum withheld to the Treasury in April. Taxpayers, however, working for employers who do not employ regular staff and those who draw their pay directly abroad are required to make a declaration of income to the authorities.

The tax varies with the taxable income. It is very light on retiring pensions and workmen's wages, heavier on the salaries of public officials and heavier still on the remuneration of other employees. In all cases, however, the burden is comparatively light. Further, the law provides a tax-free minimum of 1,500 drachmas a month or 60 drachmas a day in the case of workmen.

When salaries and wages, however, exceed twice the minimum exempt from tax on total income, the excess is liable to the tax of the employer's category.

On the other hand, when wages and salaries are paid abroad, any foreign tax paid thereon is deducted from the tax payable in Greece (see page 158).

TAX ON INCOME FROM THE LIBERAL PROFESSIONS.

It has already been mentioned (page 164) that the taxation of this income is governed by a dual system of *patente* tax and tax on net income of Category G.

(a) *Patente Tax on the Liberal Professions.*

The liberal professions are subject to the same rules in regard to *patente* tax as commercial and industrial enterprises, the only difference being that the tax of each class is in their case less by one-fifth.

In the case, however, of architects and engineers, the *patente* tax is fixed at 8 per cent of the remuneration to which they are legally entitled for plans and survey work. The tax is collected by the authorities at the source when approving the plans.

(b) *Category G Tax on Net Income.*

As mentioned above, Category G tax is imposed on annual income from the liberal professions exceeding 300,000 drachmas. This schedule also includes any income not classifiable under another category. The net taxable income is determined by deducting from gross income all taxes, charges, duties or other expenses incurred in earning the income.

Any tax paid abroad on income earned in a foreign country is deducted from the tax payable in Greece.

Taxpayers liable to this tax must declare their net income to the authorities in April, and the latter may assess with the help of advisory committees in the same way as for Category D income (see page 169).

COMPLEMENTARY TAX ON TOTAL NET INCOME.

Taxable Amount.

The total income liable to this complementary tax, which, be it remembered, is only levied upon individuals domiciled or resident in Greece, is made up of all income, whether derived from Greek or from foreign sources. It is computed as follows :

Income which has already paid Categories A and G tax and the *patente* taxes is added together. When income has been taxed on an assumed sum (*i.e.*, income liable to a *patente* tax), this assumed amount serves also as the basis for purposes of complementary tax. The Administration is free, however, to show, if it can, that the actual income is in excess of that amount and the taxpayer may adduce proof that it was less or that there was even no income at all, but a loss (see page 166). In the case of agricultural income, the tax on which is assessed on gross output, complementary tax is computed on net income as determined by the ordinary rules of agricultural accountancy. The exemptions from the schedular taxes enjoyed by certain forms of income do not apply to the complementary tax, and all such income is reckoned in for the purpose of determining the total sum liable to the latter tax. Also, any income earned by an individual abroad is liable, as previously mentioned. Accordingly, the taxpayer must include it in his declaration and the tax paid thereon abroad is deducted, not from the tax owing in Greece, but from the amount of taxable income.

A woman is not regarded as liable to tax apart from her husband ; her income is added to his.

The tax is assessed on the basis of declarations made by the taxpayer in April and duly checked by the Administration.

Deductions and Relief.

In order to determine the amount actually taxable, the following deductions are made from total net income :

- (a) Losses sustained on any class of income, whether in Greece or abroad ;
- (b) Taxes already paid on the income in Greece and taxes paid abroad ;
- (c) Life or accident insurance premiums paid under insurance policies issued in the name of the taxpayer or of any of his dependents ;
- (d) Interest on debts of the taxpayer or his wife ;
- (e) All losses from the destruction, dwindling or permanent depreciation of capital, if incurred during the two years preceding the tax-year and if not covered by donations, legacies, dowries or an appreciation of other capital assets.

From the total net income thus obtained, 100,000 drachmas are deducted as tax-free. This exempted minimum is increased by 3,600 drachmas for each person dependent upon the taxpayer.¹ Tax, computed on a sliding scale, is then levied upon the taxable income thus obtained.

Exemptions.

The following persons and income are exempt :

- (a) Subject to reciprocity, income received from foreign sources by foreigners settled in Greece ;
- (b) Subject to reciprocity, foreign diplomatic and consular agents ;
- (c) War pensions ;
- (d) The coupons of certain Greek loans.

Taxable Minimum.

The taxable income of individuals must not be less than a certain assumed figure based upon certain indices. This figure is obtained by first applying a certain coefficient to the rent of the house or houses occupied by the taxpayer. This coefficient varies ; as regards houses subject to the moratorium on rents, the assumed income is between five and seven times the rent, according to the amount of the latter. In other cases, the income is assumed to be from three to seven times the rent. The income as assumed from the rent is increased by : (a) 30,000 to 100,000 drachmas for each motor-car belonging to the taxpayer ; (b) 50,000 drachmas for each motor-boat of more than 20 h.p. ; (c) 100,000 drachmas for each yacht.

The taxpayer is not permitted to show that his actual income is smaller than the figure resulting from the indices or that he has sustained a loss. In quite exceptional cases, however, the index figure may be reduced for persons whose income is derived from interest on certain Greek loans. Further, although not at liberty to plead a smaller income figure than that furnished by the indices, the taxpayer must declare his actual income if it is larger than the assumed figure.

4. DECLARATIONS, APPEALS AND COLLECTION.

For purposes of taxes on net income from leased land, foreign securities, industrial and commercial enterprises, agriculture and the liberal professions and for purposes of the tax on total income, taxpayers have to declare their income to the Administration in April of each year. Also any individual or legal entity who has withheld tax from income paid to third parties (personal securities, salaries and wages) must declare these sums in April.

With regard to other taxes, either no declaration is required or it is not required every year.

The following are the detailed rules on this point applying to each tax :

As the buildings tax remains fixed for a certain period following each assessment, owners whose liability continues need only furnish a declaration to the authorities when it has been decided to reassess for a fresh period. At other times, declarations are only required if the taxable income has increased or diminished by more than 10 per cent since the last assessment.

The *patente* taxes and the taxes on commercial occupations and the liberal professions being assessed every three years, taxpayers have, as a rule, to make declarations only at the beginning of

¹ By person dependent upon the taxpayer is meant : (a) wife (always) ; (b) mother, father, unmarried daughters and sisters, sons not of age or incapable of earning their living and brothers of husband and wife not of age, if they have no means of their own and are living with the taxpayer.

each triennial period. In other cases, when *patente* tax is levied (tobacco, shipping, companies), the taxpayer submits an annual declaration.

As regards taxes on the different products of agriculture, when these are collected and assessed like indirect taxes or at a flat rate, taxpayers have to make their declaration to the Treasury at the time when the tax becomes payable — that is to say, at the time of production, sale or export, according to the commodity.

Declarations are, of course, checked, either by the Administration or by special committees, as stated above.

Should the declaration be found insufficient or inexact, the taxpayer may be asked to furnish explanations and confirmatory evidence. If no declaration is made or if the additional information supplied by the taxpayer does not satisfy the authorities, the latter may assess on such data as they think trustworthy.

The taxpayer may then appeal against their decision to a committee consisting of a civil court judge, a revenue official and a representative of the taxpayer, such appeal being lodged within twenty days of receiving the assessment notice. Both the taxpayer and the Administration may appeal against the committee's decision to a committee of second instance — if the disputed tax does not exceed 20,000 drachmas — or to a department of the Court of Auditors, if a larger sum is involved. Moreover, the decisions of this second instance may, at the request of either party, be quashed by the Council of State, which in this matter plays the part of Court of Cassation.

The tax is collected in four instalments, the first in April at the time of declaration, the second in July, the third in October and the fourth in January. These periods do not apply to the taxes on the various agricultural exports, which are collected in cash at the time of determining the taxable income, or to taxes deducted at source, which are paid to the Treasury in April by those who withhold them.

PART II. — METHODS OF TAXING FOREIGN AND NATIONAL ENTERPRISES.

A. FOREIGN ENTERPRISES.

I. DEFINITION AND GENERAL PRINCIPLES.

Foreign enterprises are, in principle, liable to taxation in Greece in so far as they benefit from an income having its source in that country.

Enterprises belonging to individuals or to partnerships are regarded as foreign if their real centre of management is situated abroad.

As far as enterprises belonging to share companies are concerned, they are considered as foreign if the share companies to which they belong are organised in accordance with the laws of a foreign country.

In order that foreign enterprises may be taxed on their industrial and commercial profits, it is an indispensable condition that they should possess in Greece either a local branch or a representative or agent.

Foreign salesmen, representatives and commission agents travelling in Greece are also liable to taxation in respect of business transacted by them in that country.

When the enterprise is established as a share company, it is liable to the tax on net income belonging to category D. In exceptional cases, the category D tax may be replaced by that on category C income (see page 159). In all other cases, foreign enterprises are liable to the *patente* tax on profits not exceeding 300,000 drachmæ and to the tax on net income (category D) on income exceeding that amount (see page 169).

Foreign enterprises, whatever their form, which realise commercial or industrial profits abroad through branches, agencies, or representatives and which depend upon or are effectively controlled in Greece, are liable to the aforementioned taxes on their foreign profits. But any tax paid abroad on this same income is deducted from the total tax payable in Greece, but such deduction must, of course, not exceed the amount of the total tax (see page 163). Enterprises may, however, as already indicated at that page, be completely exempted from taxation of this income from foreign sources, subject to reciprocity.

Profits from a Greek source earned by vessels flying the flag of one of the countries with which Greece has signed a reciprocal exemption treaty are tax-free.

Foreign enterprises deriving from a Greek source income falling under categories A, B, C and E, are, in principle, liable to the taxes applicable to these categories, notwithstanding that they have no branch, agency or representative in Greece.

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) *Dividends.*

Dividends paid by national share companies are liable to the tax on class (a) of category C, the tax being collected by withholding at the source ; foreign enterprises in receipt of this kind of

income are taxable, irrespective of whether or not they have an office in Greece (see page 161). An exception is made in regard to dividends paid by certain specified share companies which, under a special agreement with the Government, are exempt from all taxation.

Dividends paid by foreign share companies are liable to the tax on class (b) of category C in the following cases :

(1) Where the dividends are paid in Greece or received through a banking establishment in Greece, independently of whether or not the foreign enterprise to which they accrue has an establishment in Greece ;¹

(2) Where, although such income is received directly abroad, it accrues to an establishment of some kind situated in Greece.

The fiscal exemption of income from a foreign source is, however, possible, subject to reciprocity (see page 159).

(b) *Interest.*

A distinction is made between interest from loans in the form of bonds belonging to classes (a) and (b) of category C and other interest, including that on mortgage or other (*i.e.*, that on deposits, accounts receivable, credits, secured or unsecured loans) which constitutes class (c) of category C.

Coupons of bonds issued by Hellenic legal entities and companies, as well as interest of any other sort from a Greek source, are, in principle, liable to the tax, regardless of whether the enterprise in receipt thereof has an establishment in Greece or not. There are, however, so many exceptions to this rule that interest on capital of any sort imported from abroad is actually tax-free. Thus, the following income, irrespective of whether the foreign enterprise to which it accrues has an establishment in Greece or not, is tax-free.

(1) Coupons of loans to the Government, communes, municipalities and harbour authorities ;

(2) Coupons of bonds issued by national industrial companies, in so far as this interest has not been deducted from income subject to the tax on buildings belonging to such companies ;

(3) Coupons of bonds and interest on loans of all kinds contracted by enterprises which exploit lignite mines in Greece ;

(4) Coupons and interest of all kinds on loans contracted by certain specified companies exempt from taxation under a special agreement with the Government ;

(5) Interest on bank deposits with Greek banks.

The following income is also tax-free in so far as it is derived from capital furnished by individuals or enterprises established abroad :

(1) Interest on credits and remittances in general granted abroad to national and foreign banking institutions in Greece. The rate of interest thus exempted may not exceed the official discount rate of the country whence this capital is derived. Exceptionally, in the case of establishments exclusively furnishing loans on tobacco, the exempted rate may not be less than 5 per cent.

(2) Coupons and interest of all kinds on loans from abroad made to share companies or other enterprises of a certain magnitude in Greece, in so far as such interest has not already

¹ As mentioned on page 161, note 4, the Administration has issued instructions prescribing that no tax should be levied when the recipient of the income has no domicile or has not resided six months in Greece.

been deducted from the income subject to the tax on buildings belonging to the debtor company or enterprise.

(3) Interest on credits granted abroad for the purpose of facilitating the importation of goods or the exportation of agricultural and stock-breeding products, treated or otherwise; due proof of the purpose of these credits is required.

(4) Interest on foreign loans granted on the security of Hellenic ships.

Foreign coupons accruing to foreign enterprises established in Greece are by analogy subject to the rules governing dividends from the same source.

Interest from abroad is liable to taxation in so far as it accrues to a Hellenic establishment of a foreign enterprise (see page 162); the latter may be fully exempted, subject always to reciprocity.

(c) *Directors' Percentages.*

Directors' percentages paid by Greek companies to directors are taxed as dividends.

(d) *Royalties for Use of Patents, Copyrights, Trade-Marks, Secret Processes and Formulæ and Other Income from Personal Property.*

Authors are, in principle, liable to the *patente* tax on the liberal professions and to the category G tax (see page 164) in respect of income accruing to them personally from their published works, whether directly or through some third person. Income accruing to their heirs from the same source is liable to the category G tax, it being considered as income which may not be subject to tax under any other category.

Authors in receipt of income from abroad are also taxed thereupon, if domiciled in Greece or resident there for six months. They are, however, entitled to deduct from the tax payable in Greece any tax paid abroad. Foreign authors living in Greece and in receipt of income from abroad may be exempted on a basis of reciprocity.

Authors or their heirs living abroad, in receipt of income in Greece, are liable to the *patente* tax and the category G tax.

The above provisions in connection with authors, it should be observed, have never been applied by the Administration, which, on account of the small incomes earned by authors, has made a rule of not taxing them.

The net profit accruing to licensees of copyrights is treated as commercial profit and is liable to the *patente* tax, together with category D tax, or, as the case may be, to the share companies tax of category C.

Income from patents is, in principle, liable to the category G tax (on liberal professions) it being considered as an income which does not fall under any other category.

Where the inventor exploits his patent directly, either alone or in collaboration with others, his income is treated as commercial profit and is liable to the *patente* tax and the category D tax. Where the inventor is in receipt of commercial income from abroad, he is, by analogy, subject to the provisions concerning authors. Inventors domiciled or resident abroad are taxable in respect of income earned in Greece.

Where authors or inventors cede their respective rights or patents to third persons, profits accruing under the cession are liable to the category D tax. Only four-fifths, however, of this income is taxed (see page 169), the income being regarded as capital profit.

Finally, profits accruing from the cession of rights in general, as, for instance, leaseholds, goodwills, etc., are liable, up to four-fifths of their amount, to the category D tax, in so far as the income has its source in Greece and irrespective of the domicile or seat of the recipient.

In all the aforementioned cases, the tax is arrived at on the basis of the taxpayer's return, which is verified by the Administration.

(e) *Rents from Real Estate, Mining Royalties and Similar Income.*

Income from buildings is liable to the category A tax.

As regards land, it may be recalled that there is no general land tax on income from land. Only leased land is liable to the category B tax on the net income. Agricultural concerns are, however, liable in a general way to taxation, but the tax is assessed on the gross income, except in connection with stock-breeding, and varies according to the nature of the produce.

Royalties or rents paid by mining concerns in Greece to persons abroad from whom they hold concessions are liable to the special tax on mining royalties. Furthermore, concessionaires are required to pay the "area" tax.

(f) *Gain derived from the Purchase and Sale of Real Estate, Securities and Personal Property.*

In so far as casual and non-habitual transactions are concerned, the profits accruing from operations in real or personal property, tangible or intangible, are, in principle, not taxable.

If a foreign enterprise deals professionally in the purchase and sale of personal or real property through its own office or representative, or through an agent, etc., it is subject to the *patente* tax and to the tax on category D income, which are applicable to commercial enterprises.

Gains from movable capital employed by the branch in Greece of a foreign enterprise are taxable up to four-fifths of their amount if they are merely occasional.

Profits of the same kind accruing to such branch from a foreign source are likewise taxable. However, the tax which may have been paid abroad on such income is deducted from the tax payable in Greece. If, however, there is reciprocity of treatment, they may be exempted from the tax.

(g) *Salaries, Wages, Commissions and Other Remuneration for Services.*

Salaries and wages are subject to the category F tax, and remuneration in the liberal professions is subject to the *patente* tax and to the category G tax. Where the income is earned in Greece, it is taxable whether or not the recipient is established in Greece. Income of these two categories earned abroad by persons domiciled in Greece or resident there for not less than six months is also taxable. However, it is necessary to deduct from the tax due in the country any tax already paid abroad on such income.

Total exemption is granted when there is reciprocity.

(h) *Income from a Trust.*

The trust is not itself subject to taxation ; it is the beneficiary who is taxed. In the case of schedular taxes levied irrespective of the domicile of the recipient of income (for example, taxes of the categories A, B, C, and E), tax is levied in all cases without exception ; but, where domicile or a residence of six months in Greece is a necessary prerequisite for assessment, the tax is levied only where the beneficiary fulfils these conditions.

(i) *Income from the Carrying-on of a Business or Industry.*

In principle, a fiscal obligation rests on foreign enterprises when they possess in Greece a permanent establishment — *i.e.*, a branch, shop, office, or any industrial establishment whatsoever (factory, mine, workshop, etc.). In all other cases, it is a question of fact whether or not a foreign enterprise is liable to taxation.

Where a foreign enterprise transacts business in Greece through a *commission agent or broker*, even though it makes occasional consignments of merchandise for sale, it is not, in principle, liable to taxation. Where, however, the enterprise authorises an agent to sell on commission goods out of a stock in Greece belonging to the foreign enterprise, the latter is liable.

If goods belonging to the foreign enterprise are bought for sale in the home market by a local dealer or distributor who has an exclusive right to market them and who is trading on his own account, no fiscal obligation rests on the foreign enterprise.

Where an agent (*représentant*) is engaged solely in collecting orders for, and transmitting them to, an enterprise abroad, the latter is not liable to taxation in Greece. If, however, it appears from the manner in which the transactions are conducted that the representative is empowered to conclude sale contracts binding upon the foreign enterprise, the latter is taxable. Similarly, where the operations of the representative or agent are such as to make him the employee of the foreign enterprise, the latter is taxable, as it is deemed to have a permanent establishment in Greece.

Foreign *commercial travellers* are not, in principle, taxable. However, when they conclude contracts in Greece, a fiscal obligation arises.

Wherever the above fiscal obligation exists, the agents or representatives are required to submit a return in respect of their personal profits and commissions, together with a separate return in respect of the foreign enterprise, whenever the latter is taxable.

B. NATIONAL ENTERPRISES.

Enterprises belonging to individuals or to partnerships are national when their real centre of management is situated in Greece. In so far as enterprises belonging to share companies are concerned, they are considered as national if the company to which they belong is organised under Hellenic law.

Cases where national enterprises in receipt of profits from abroad are liable to tax are not very numerous. Thus, certain kinds of income, such as that derived from real estate, are completely exempt. Other kinds, such as income derived from business enterprises, salaried occupations and liberal professions, are, in principle, taxable in Greece; but the amount of tax paid abroad on such income is deducted from the tax due in Greece, so that, in fact, these categories too may be regarded as exempt. Only income from foreign securities is always taxed.

(a) AND (b) DIVIDENDS AND INTEREST.

Dividends and coupons, which are comprised in class (b) of category C (see page 161), are taxable if paid in Greece or if they are received through a banking establishment in Greece.¹ This tax is collected at the source, the agent of payment being bound to withhold the tax and pay it to the Treasury in the month of April of the following year. Dividends and coupons which are received abroad by the recipient himself and other interest from a foreign source — that is, class (c) interest — paid direct or through a Greek banking establishment, are taxable only if the recipient is domiciled in Greece or has been resident there for six months. The tax is payable by the taxpayer himself, who has to submit a return relative thereto. Where the recipient of such income is a foreigner, he may be exempted from taxation, subject to reciprocity. The taxable income is checked mainly on the basis of the books kept and other information supplied by the taxpayer himself, together with other data in the hands of the fiscal authorities, such as the returns made in connection with capital and succession taxes.

¹ It should be remembered (see note 4 on page 161) that the Administration imposes the tax only in the case where the recipient of the income has his domicile or has resided six months in Greece.

(c) DIRECTORS' PERCENTAGES.

Directors' percentages which are paid by foreign companies to Hellenic enterprises are subject to the same fiscal treatment as foreign dividends.

(d) ROYALTIES FOR USE OF PATENTS, COPYRIGHTS, TRADE-MARKS, SECRET PROCESSES AND FORMULÆ AND SIMILAR INCOME.

The income which authors receive from abroad in connection with their copyrights is subject either to the tax on category G or category D. In the case of authors' heirs, such income is taxable only if it falls under category D. The tax paid abroad on such income is deducted from the amount payable in Greece, with the result that, actually, it is very rarely taxed in Greece. Inventors, in so far as they are liable to the category G tax, are not taxable in Greece in respect of their income from abroad. If, however, the income comes under category D, the recipients of such are taxable, but tax is, in fact, very rarely levied, since the tax paid abroad is deducted from the amount due in Greece.

It is, of course, necessary, in order that there should be tax liability in the above cases, that the party concerned should be domiciled or resident in Greece for six months.

(e) RENTS FROM REAL ESTATE, MINING ROYALTIES AND SIMILAR INCOME.

Income from buildings or land situated abroad is not liable to schedular taxation. On the other hand, income from mines and quarries is liable to category D tax as income from commercial enterprises, and the taxes which have been paid abroad on such income are deducted from the amount payable in Greece. This income is checked mainly on the return and information furnished by the taxpayers themselves.

(f) GAIN DERIVED FROM THE PURCHASE AND SALE OF REAL ESTATE, SECURITIES AND PERSONAL PROPERTY.

Income derived from transactions in personal or real property, tangible or intangible, is taxable in Greece if it may be considered, according to what has been said on page 177, as part of the income of a commercial or industrial enterprise subject to the tax on category D. As mentioned above, tax paid abroad is deducted.

(g) SALARIES, WAGES, COMMISSIONS AND OTHER REMUNERATION FOR SERVICES.

Remuneration for services rendered abroad is taxable in Greece if the recipient is domiciled or has resided there for six months. In such cases, it is subject, according to its nature, to the tax on category F or on category G. As already indicated, tax which may have been paid abroad is deducted from the amounts payable in Greece, the result of this is that it is rare that such income is actually taxed.

(h) INCOME FROM A TRUST.

See in connection with the taxation of trusts what has been said under the corresponding heading of Section A of this part.

(i) INCOME FROM THE CARRYING-ON OF A BUSINESS OR INDUSTRY.

As was explained with reference to the taxation of profits from commercial and industrial enterprises, income derived by enterprises of this kind from abroad through branches, agencies or representatives which depend upon an enterprise situated in Greece, or are controlled from the country, are also taxable. Any tax paid abroad in respect of such income is, of course, deducted from the tax payable in Greece.

PART III. — METHOD OF ALLOCATING TAXABLE INCOME.

A. FOREIGN ENTERPRISES WITH LOCAL BRANCHES OR SUBSIDIARIES.

I. GENERAL QUESTIONS AND METHODS OF APPORTIONMENT.

With certain kinds of income, the totals earned in Greece are clear and definite and are taxed in their entirety. Such is the case with income from buildings (category A), income from leased land (category B), income from Greek securities (category C, class (a)), interest from Greek sources (category C, class (c)) and profits from agricultural concerns situated in Greece (category E).¹ In these cases, the tax is imposed irrespective of the taxpayer's domicile. It therefore applies equally to foreign enterprises in Greece. Of course, there are exemptions from this tax ; these are indicated in the first part of the study in the sections dealing with each kind of income. But where the tax is applicable, no doubt arises as to the income taxable. Some difficulty exists in determining income from Greek sources in categories F (salaried occupations) and G (liberal professions). But, as cases of this kind only rarely arise, there have been no serious disputes, and it has not been difficult for the Administration to agree with the taxpayer.

The question has not been so easy in the case of commercial enterprises, and the solutions reached in regard to the various kinds of enterprise will be described hereafter.

As regards methods of reckoning profits, it may be pointed out here that the legal provisions governing foreign enterprises are not always explicit. They have, however, been supplemented by judicial decisions and administrative practice, which tend to bring them under the general rules applicable to all enterprises.

Some enterprises, notably mining concerns, although, in their essence, national enterprises, have preferred to assume the form of foreign share companies. Their head offices are abroad, but their main field of operations lies in Greece. As a concession to these companies, they have, at their own request, and with the approval of the Ministry of Finance, been assimilated, for fiscal purposes, to national companies ; once this assimilation has been granted, it must remain effective for three years. In this way, they are privileged, not only to deduct from profits earned in Greece the whole of their expenses and losses abroad, but also to be taxed only on their distributed dividends instead of on the whole of their earned profits. Thus no question of allocation arises.

(a) BOOK-KEEPING AND ACCOUNTING REQUIREMENTS.

No special provisions apply to foreign enterprises in connection with their accounts and book-keeping. Such enterprises are, therefore, subject to the general rules laid down by the Commercial and Civil Procedure Codes. In addition, the provision of the fiscal law, which requires the taxpayers of category D to keep a day-book and to enter in such ledger certain data and information, also applies to foreign enterprises.

¹ As regards agricultural concerns, the tax is sometimes on net income, sometimes on gross.

(b) METHODS OF ALLOCATION.

I. *Method of Separate Accounting.*

In principle, this method is preferable, because it follows with regard to foreign enterprises exactly the same rules as are applied to national enterprises. The Administration seeks to determine the profits taxable according to this method, even when accounts have not been fully kept, provided that sufficient information is available to enable it to employ this method. This, however, gives rise to differences of opinion between the fiscal authorities and enterprises in regard to the data necessary to arrive at the taxable income.

In this connection, the chief difficulty is the checking of the invoice price of imported goods, the price appearing in the books being often conventional. In this, the Administration is guided by the relations between the branch in Greece and the establishment abroad, and by the general conduct of the enterprise, and it seeks to determine the real cost price of goods to the foreign establishment ; to this price, a reasonable percentage is added in order to cover the profits of the establishment furnishing the goods ; thus an invoice price approximating to the foreign market price is obtained and to this price is, of course, added the freight and other similar disbursements. In principle, the Administration is satisfied with the foreign exporting establishment's accounts. Where, however, these are unsatisfactory, it relies on other data and documents, furnished by the enterprise itself — e.g., quoted prices or sale prices to independent customers, etc., furnished by the enterprise itself. If the result is uncertain, recourse is had to a comparison with national enterprises of the same character, if any ; the price paid by the latter for purchases abroad is deemed to be the invoice price of the foreign enterprise. In the absence of such data, an amicable arrangement is always sought ; this may be based either on a price reckoned in accordance with information from enterprises different in character but similarly situated, or on any other reliable information ; in view of the fact that the Administration is entitled to employ yet other methods explained below in order to determine the taxable income, it frequently happens that an agreement as to the invoice price is reached with the taxpayer.

Enterprises other than importing firms also give rise to difficulties, sometimes equally great. These are treated in a manner similar to that explained above.

Another subject of dispute between the taxpayer and the Treasury concerns the apportionment to the branch in Greece of the overhead and other expenses of the head office. This difficulty does not, of course, arise where accounts are based strictly on market conditions in Greece, or when the invoice price is fixed in the light of conditions prevailing among national enterprises. Sometimes, however, accounts, although independently kept, are such that an examination of the allocation of expenses is inevitable. If there is sufficient data available, the expenses of the local branch are considered by themselves. Otherwise, recourse is had to steps similar to those noted above — e.g., comparison with national enterprises, etc. ; at other times, the analogy method discussed in (c) below is applied.

2. *Empirical Methods.*

Percentage of Turnover Method. — In the majority of cases, the only exact and determinable factor is the Greek turnover of the foreign enterprise. The other factors for fixing profits can be checked only with great difficulty. In these cases, the profits taxable in Greece are determined by multiplying the turnover by a special percentage. This percentage is contained in a table framed by a special committee which fixes a minimum and maximum percentage for each kind of

enterprise.¹ In each case, the fiscal authorities decide on the percentage which they think suitable, within the limits, of course, of the maximum and minimum fixed. For this purpose, they take into account the profits ordinarily realised by national enterprises of the same character. It is, however, open to foreign enterprises to show that the actual percentage of profits is lower than the minimum fixed; similarly, the fiscal authorities are entitled to show that the real percentage of profits is higher than the maximum fixed in the table.

Method of the f.o.b. Price. — This method is used for foreign enterprises engaged in producing or merely in treating raw materials or merchandise for final sale abroad. It consists in determining the increase of value which results for the goods from the treatment given them by the enterprise concerned in Greece. If the appreciation exceeds the working expenses incurred in Greece, there is a profit on such goods. This profit, although it only becomes effective when the goods are sold abroad, is taxable in Greece because it was created in that country. This method is applied mainly to the tobacco enterprises. Recently, a special law has altered the system of taxing tobacco; consequently, the method is now only very rarely used.

Method of a Commission on the Cost Price. — This is applied in the same cases as the previous method; it presupposes that it is impossible to determine the gross income because sales are effected abroad. The assumption underlying this method is that foreign enterprises established in Greece with a view to producing or treating, etc., various products, not only enjoy the advantages resulting from personal supervision, but save the commissions which they would otherwise have to pay to some national enterprise. Nevertheless, with a view to encouraging and assisting these foreign enterprises, which help to develop the export of Greek products, the Government taxes them only on a fixed commission, this commission being calculated on the Greek cost price and the percentage applicable to each category of enterprise as fixed by the special committee. The recently adopted method of taxing tobacco concerns is based on the same principle.

3. *Method of Fractional Apportionment.*

This method is not so frequently used as the others. It applies mainly to enterprises not engaged in marketing foreign products in Greece. It consists in determining, first of all, the ratio of the net profits to the gross income of the enterprise as a whole, as shown by the general balance-sheet of the central establishment. Applying this ratio to the accounts of the Greek branch, the net profit corresponding to the gross income of the Greek branch is arrived at.

Generally speaking, the Administration considers that it comes nearer the mark if, instead of seeking to determine directly the final net profits, it proceeds in a more analytical manner and takes into account in its computation the different items of liabilities and assets which go to make up the

¹ The following percentages may be given as examples :

	Percentage
Wholesale coal-merchant	2-6
Wholesale colonial produce merchant	1-2
Wholesale grain merchant	2-6
Wholesale petrol and oil merchant	2-7
Wholesale textile merchant	4-10
Wholesale scrap-iron dealer	2-7
Automobile dealer	7-17
Sewing-machine dealer	7-14
Watchmaker	9-21
Cattle dealer	2-6
Druggist	4-14
Dealer in machinery and tools	6-14

net profits. Thus, the Administration seeks to establish the relations existing between the debts of the branch and of the head office, particularly as regards commissions, interest, insurance premiums, sales of goods exported from the country, together with general overhead expenses, interest and commissions paid out, sinking funds and reserves, etc. This detailed method is preferable, since establishments abroad very often transact different kinds of business and have more or less varied objects. To establish these comparisons, account is sometimes taken of the capital in the business if there is a fixed ratio between the capital belonging to the foreign enterprise as a whole and the capital used by the latter in Greece. In other cases, where goods of a certain kind are dealt in, an attempt is made to determine the ratio between the quantity of the goods sold to Greece and the total quantity sold by the enterprise as a whole.

4. *Requirements for Selection of Methods and Value of the Various Methods.*

As stated above, the method of separate accounting is, as a rule, preferable. Where this method is not applicable, the percentage of turnover method is adopted. Both methods, and especially the former, have the merit of confining the enquiry to wholly Greek transactions, and of not being influenced by the results of the enterprise's foreign establishments. Thus, where the local establishment earns certain profits, it is unfair that these should be diminished by losses of other establishments situated abroad. Conversely, where the local branch incurs losses, it is unjust that it should be taxed in respect of profits exceeding those losses earned by other foreign establishments.

Where the Greek taxable profit is fixed as a fraction of the foreign enterprise's total profit, these two difficulties are unavoidable. While, therefore, this method is sometimes used in Greece, its use is restricted to cases where satisfactory results are unattainable by the methods of separate accounting and percentage of turnover. The methods of the f.o.b. price and the commission on cost price are applicable only to special cases, where, however, they are preferable to any other, apart, of course, from the method of separate accounting. Tobacco enterprises are an exception, the only method applicable to them being the method of commission on cost price.

In general, the method of taxation followed by the Administration is that of separate accounting, except where the law prescribes a special and exclusive method — as, for instance, in connection with the tobacco trade. Where, however, the method of separate accounts is not satisfactory, the Administration may employ others. It should nevertheless be pointed out that, both in law and in administrative practice, the aim is to afford foreign enterprises every possible facility for arriving at a reasonable figure for taxable profits.

It should also be noted that the right accorded to foreign share companies to be assimilated for fiscal purposes to national share companies gives the former a kind of choice in regard to the method of allocation of taxable profits. In connection with the application of these provisions, it should be observed that an agreement is necessary between the enterprise and the Administration, the latter's consent, however, being readily granted to the proposals put forward by the enterprise.

(c) APPORTIONMENT BETWEEN BRANCH AND PARENT ENTERPRISE.

I. *Apportionment of Gross Profits of Branch to Real Centre of Management abroad.*

In principle, none of the profits of the branch are attributable to the real centre of management situated abroad. The whole of the profits earned in Greece by foreign enterprises is taxable. Only a proportion of the general expenses incurred by the management abroad may be apportioned as charges incurred in connection with the branch in Greece.

2. *Apportionment of Expenses of Real Centre of Management to Branch.*

Interest Charges.

Where capital borrowed by the enterprise has clearly been devoted to the use of the establishment in Greece (for instance, industrial plant, railway construction, etc.), interest on these loans is chargeable to that establishment. The same rule applies when only a part of the loan has been invested in Greece, and, in this case, the branch is considered as having assumed the portion of the interest which corresponds to the amount invested in Greece. It should, however, be recalled that interest on capital imported from abroad is tax-free.

General Overhead.

There is no allocation of the general overhead of the principal enterprise where the establishment in Greece is a subsidiary. Further, in the case of branches having separate accounts, the general overhead of the principal enterprise is not taken into consideration when goods and capital sent from abroad have been debited at a price inclusive of a proportion of head-office expenses. In other cases, a proportion only of the foreign central establishments expenses are chargeable to the branch in Greece — viz., those relating to central administration (for instance, expenses of the board of management, director-general's fees, etc.), centralisation of accountancy, inspection and other services of a similar character. The proportion of the expenses to be borne by the branch is usually fixed on the basis of the relation existing between its gross income and that of the enterprise as a whole. It may, however, be based on other factors more in keeping with the relations existing between the branch and the real centre of management — for instance, assets, plant and equipment, etc.; sometimes a comparison with local enterprises of a similar character serves as a basis for the apportionment of overhead expenses.

3. *Apportionment of Net Profits of Branch to Deficitary Parent and vice versa.*

Where the branch or subsidiary in Greece operates at a profit, whereas the enterprise as a whole works at a loss, no account is taken of that loss in determining the income of the branch or subsidiary; the whole of the profits realised in Greece are taxable. Indirectly, however, this rule is departed from when the method of fractional apportionment is applied.

The above rule applies where the branch or subsidiary in Greece works at a loss, whereas the enterprise as a whole makes a profit; the results of the enterprise in Greece are treated separately. No profits being earned in that country, no taxation is imposed. Again, however, the application of the method of fractional apportionment marks a departure from this rule (see pages 183 and 184).

(d) APPORTIONMENT BETWEEN PARENT ENTERPRISE AND SUBSIDIARIES.

Subsidiary companies are Hellenic share companies whose shares are mainly or entirely held by foreign enterprises, by which they are generally formed. Subsidiary companies, since they are distinct legal entities, are treated as separate economic units which transact business with the parent enterprise abroad just as they do with third parties. This manner of doing business in Greece gives the greatest facilities for the keeping of a separate accountancy for the purpose of determining the profits realised in Greece. Since, however, to all external appearances, subsidiaries are unconnected

with an enterprise abroad, goods sent to them by the parent company may well be invoiced at very high prices which the Administration cannot readily check. There is no explicit provision governing the case where one of the two contracting enterprises is a subsidiary of the other. However, this question is of little importance at present, as share companies are taxed on their distributed profits and not on those actually realised. Consequently, there have been no difficulties in this connection between the Administration and the companies in question. It should be noted that, just as in the case of other national companies, where a subsidiary organised at a date later than April 1st, 1926, distributes a dividend amounting to less than 5 per cent on its share capital, it may be assessed for the category D tax ; in this case, should the subsidiary company's accounts not be satisfactory, the Administration may follow the methods described above in order to fix its taxable income.

II. APPLICATION OF THE METHODS OF ALLOCATION IN SPECIFIC CASES.

(a) INDUSTRIAL AND COMMERCIAL ENTERPRISES.

I. *Selling Establishments.*

Local Establishments selling in National Markets.

Foreign enterprises which have in Greece a permanent establishment selling goods despatched to it from abroad are taxed on their net income realised in the country. This income is determined by one of the following methods : separate accounting, percentage of turnover or fractional apportionment. Where the Greek establishment takes the form of a subsidiary company, it is separately treated as a Greek share company.

Local Establishments of Foreign Enterprises selling abroad.

If an enterprise whose real centre of management is situated abroad possesses in Greece a branch which sells in a third State where the enterprise has no permanent establishment, the profits from such sales are considered as being derived from Greece and are therefore taxable. The tax paid abroad is, however, deducted, and, subject to reciprocity of treatment, the enterprise may be exempted from tax.

2 and 3. *Manufacturing and Processing Establishments.*

As explained above, a fiscal obligation rests on foreign enterprises engaged in Greece in producing, or merely treating, raw materials or goods. Their taxable profits, when not determinable by separate accounting, are fixed according to one of the following methods : fractional apportionment, f.o.b. prices, commission on cost price. When fractional apportionment is employed, the total profits are divided on the basis of the proportion of the turnover on sales of goods exported from Greece to the turnover on other sales, and the fraction of the net profits corresponding to the amount of the sale of Greek goods is regarded as the taxable income. Where the second of the above methods is used, the f.o.b. price of the exported goods is taken as gross income and the net profit is determined in accordance with the rules usually employed when recourse is had to this method. In the third method, the profit is arrived at by applying a certain percentage of the cost price of the exported product. Tobacco enterprises are, as indicated above, subject to a system of assessment similar to the method of commission on cost price and the other methods do not apply to them.

4. *Buying Establishments.*

Enterprises regularly buying goods through a permanent establishment in Greece and selling them elsewhere are not, in principle, taxable. However, an exception is made to this rule in the

case of tobacco enterprises, which, even if they merely make purchases in Greece, are liable to the special *patente* tax on the tobacco trade. Incidentally, enterprises confining themselves to purchases alone are very few in number, and the great majority only export tobacco after treating and manipulating it. Further, in most cases, the purchasing enterprise practically passes the tax back to the enterprise which treated the goods. This is, indeed, fair, since, if the latter had itself exported the goods, it would have been taxable.

5. *Research or Statistical Establishments, Display Rooms, etc.*

An enterprise with an establishment in Greece which does not engage in profit-making transactions, but renders services to the enterprise which contribute indirectly to the realisation of profits, is not regarded as earning profits in Greece¹ and is therefore not taxable.

(b) BANKING ENTERPRISES.

The taxable profits of banking enterprises are determined by the method of separate accounting. In certain cases, however, where there are no separate accounts or where the accounts kept do not satisfy the requirements of the Administration, the gross profits and corresponding expenses are determined by any method possible. The method preferred is that of comparison with Hellenic banking enterprises in matters where such comparison is possible, as, for instance, the general expenses of the head office, etc. The question of interest to be debited or credited to the head office abroad has called for special attention. If the business of the branch in Greece is such as to lead to the importation of capital into Greece, interest debited by the head office to the branch is tax-free and this in virtue of a special provision of the law mentioned on page 162. Nevertheless, the branch, in drawing up its accounts, is entitled to include such interest as part of its expenditure and to deduct it from its gross income when determining its taxable profits. But, in order that such deduction be permissible, the following conditions must be complied with :

- (1) The rate of interest deducted may not exceed the official discount rate of the lending country, and
- (2) Such interest may not include interest on capital indispensable to the establishment of the Greek branch.

To determine the capital indispensable for establishing the business in Greece, the whole of the capital of the enterprise, including reserves, is divided in the ratio of the gross income of the enterprise in Greece to that of the enterprise as a whole.

If, on the contrary, capital is exported by the branch, the main question is what interest shall be credited to the branch, as such interest must be added to the gross income of the branch. There is no special legal provision for such a case, but the Administration holds that the rate of interest on exported capital should be estimated on the basis of the official Greek discount rate.

(c) INSURANCE COMPANIES.

Insurance companies are assessed by the method of separate accounting. The reason of this is that, as a general rule, the various items under receipts and expenditure result from business

¹ Only the *patente* tax of the lowest class, of which the rate is insignificant, is levied. In the case of share companies, the *patente* tax is of a fixed amount of 25,000 drachmæ, as stated above.

transacted in Greece. However, in regard to the allocation of mathematical reserves and other special technical reserves of all kinds, recourse is had to the method of fractional apportionment.

(d) TRANSPORT ENTERPRISES.

There are no foreign railway or motor omnibus companies in Greece. The two foreign aviation companies and a few other transport companies are exempt from taxation under special agreements. Navigation enterprises which own vessels calling at Greek ports are also taxable and the rules applying to them have been set forth in Part I (see page 163).

(e) POWER, LIGHT AND GAS ENTERPRISES.

The only foreign electrical company in Greece is exempt from taxation under a special agreement. There are a few gas companies, but their operations do not extend beyond the frontiers.

(f) TELEGRAPH AND TELEPHONE ENTERPRISES.

By a special agreement these are exempt from taxation.

(g) MINING ENTERPRISES.

There are a few foreign companies which work mines, quarries, etc. Some of them have chosen to be assimilated for fiscal purposes to Hellenic companies, and these are liable to the class (a) tax of category C (see, in reference to the conditions under which such assimilation may be authorised, page 159).

Companies having the same range of activities, but which have only their registered office abroad, are liable to the category D tax; in accordance with their request the Administration has agreed that for the determination of profits the gross income shall be reckoned, not on the f.o.b. price, but on the prices actually realised on sales abroad. It has been also agreed that all the expenses of their head offices shall be deducted from taxable profits. Hence, it may be said that, under this system, the foreign companies concerned are also assimilated to Hellenic enterprises liable to category D tax.

B. NATIONAL ENTERPRISES WITH BRANCHES OR SUBSIDIARIES ABROAD.

In principle, *national enterprises other than share companies* are liable to taxation in Greece on profits earned abroad through branches, agents, etc. However, the tax paid abroad on the taxable income is set off against the tax payable in Greece. Consequently, the allocation of profits from foreign sources is important only for the purpose of checking whether the foreign tax exceeds that due in Greece. In this case, recourse is had to calculations similar to those employed in connection with foreign enterprises, but in the contrary sense.

The same rules apply to *share companies* when they are liable to the category D tax. But, as regards share companies which are taxed on distributed profits, there is no occasion to determine their foreign profits, since there is no deduction from the taxable dividends or from the amount of the tax on the ground that profits earned abroad are included in the distributed dividends. It should be recalled that dividends of foreign share companies are, in their capacity as income from securities, subject to the tax on class (b) income of category C. Consequently, dividends derived from foreign subsidiary companies and redistributed are taxed twice.

C. HOLDING COMPANIES.

I. NATIONAL HOLDING COMPANY CONTROLLING ONE OR MORE FOREIGN SUBSIDIARIES.

As stated above, where a Greek share company is taxed on distributed profits, the latter are not subject to any deduction. Consequently, if it includes dividends from other foreign companies, already taxed as income in class *(b)*, category C, this income is subject to double taxation in Greece.

However, dividends of Greek companies already liable to the class *(a)* tax of category C may in certain circumstances be deducted from the distributed profits (see page 161).

Where, exceptionally, Greek share companies are liable to the category D tax, dividends from a foreign source subject to the class *(b)* tax of category C (in virtue of their origin) would be deducted from the net taxable income. Consequently, holding companies are taxed once on the dividends they receive from a subsidiary company, if they belong to category D, and twice if they belong to category C.

II. LOCAL SUBSIDIARY COMPANY CONTROLLED BY A FOREIGN HOLDING COMPANY.

Whether the subsidiary company be liable to the class *(a)* tax of category C on its distributed profits or to the category D tax on the whole of earned profits, the amount taxable is the product of its Greek operations and is reckoned by the methods already explained. The parent company situated abroad bears finally, like any other foreign shareholder, the burden of the tax of Category C, class *(a)* which is withheld from the dividends paid or the tax of category D which is assessed on the total profits of the subsidiary.

Annex.

TARIFF OF DIRECT TAXES.¹

	Rate of tax in percentage of the taxable income
I. INCOME FROM BUILDINGS.	
State tax	14.56
Additional taxes	6.85
	<u>21.41</u>
II. INCOME FROM LEASED LANDS.	
State tax	18.20
Additional taxes	9.75
	<u>27.95</u>
III. INCOME FROM SECURITIES.	
<i>Class (a).</i>	
(1) Dividends from Shares, Directors' and Managers' Percentages and Fees.	
<i>National Banking Companies:</i>	
State tax	20.80
Additional taxes	Nil
<i>Other National Companies:</i>	
State tax	18.72
Additional taxes	Nil

¹ The additional taxes mentioned are the taxes which are levied on behalf of public corporations other than the State on the basis of the tax paid to the latter.

	Rate of tax in percentage of the taxable income
(2) Interest on Bonds and Other Income from Class (a).	
State tax	16.80
Additional taxes	Nil
<i>Class (b). Dividends and Coupons from abroad.</i>	
State tax	16.80
Additional taxes	Nil
<i>Class (c). Interest on Debts.</i>	
State tax	16.80
Additional taxes	Nil

IV. INDUSTRIAL AND COMMERCIAL PROFITS.

(a) General "Patente" Tax.

Class of the taxpayer	Presumed income	Amount of tax
	Drachmæ	Drachmæ
First	25,000	600
Second	30,000	900
Third	35,000	1,200
Fourth	40,000	1,600
Fifth	45,000	2,000
Sixth	50,000	2,400
Seventh	55,000	2,900
Eighth	60,000	3,400
Ninth	65,000	4,000
Tenth	70,000	4,600
Eleventh	75,000	5,300
Twelfth	80,000	6,000
Thirteenth	90,000	7,500
Fourteenth	100,000	9,000
Fifteenth	110,000	10,500
Sixteenth	120,000	12,000
Seventeenth	130,000	13,500
Eighteenth	140,000	15,000
Nineteenth	150,000	16,500
Twentieth	160,000	18,000
Twenty-first	170,000	19,500
Twenty-second	180,000	21,000
Twenty-third	190,000	22,500
Twenty-fourth	200,000	24,000
Twenty-fifth	210,000	25,500
Twenty-sixth	220,000	27,000
Twenty-seventh	240,000	30,000
Twenty-eighth	260,000	33,000
Twenty-ninth	280,000	36,000
Thirtieth	300,000	39,000

(b) "Patente" Tax on Shipping Enterprises.

6.50 drachmæ for each of the first 60 tons of each vessel, and 4.50 drachmæ for each ton above 60 tons.

(c) "Patente" Tax on Tobacco Enterprises.

From 0.10 drachma to 0.60 drachma per oca, according to district.

(d) "Patente" Tax on Foreign Companies.

Foreign companies are subject to the "Patente" tax at a flat rate of 25,000 drachmæ.

(e) Category D Tax on Net Income.	Rate of tax in percentage of the taxable income
State tax	19.60
Additional taxes	4.48
	<u>24.08</u>

(f) Category D Tax applicable to Foreign Share Companies.

(1) Banks :

State tax	21.06
Additional taxes	Nil

(2) Other Foreign Companies :

State tax	18.72
Additional taxes	Nil

V. PROFITS FROM AGRICULTURAL DEVELOPMENT.

(a) Tobacco Tax.

State tax	13.70
Additional taxes	5.50
	<u>19.20</u>

(b) Tax on Oil.

(1) Tax on the Exportation of Oil from the Islands :

State tax	from 11.20 to 12.60
Additional taxes	from 4.80 to 5.40
	<u>16.00</u> <u>18.00</u>

(2) Tax applicable to Other Districts.

State tax	7.35
Additional taxes	3.94
	<u>11.29</u>

(c) *Tax on Dried Raisins.*

	Rate of tax in percentage of the taxable income
(1) <i>On the Exportation of Sultanas :</i>	
State tax	140 drachmæ for 1,000 Venetian litres
Additional taxes	42 drachmæ for 1,000 Venetian litres

(2) *Currants :*

The tax is fixed at a lump sum, which amounts to about 50 million drachmæ.

(d) *Tax on Other Agricultural Products.*

State tax	2.50
Additional taxes	0.50
	<u>3.00</u>

(e) *Tax on Stockbreeding.**Tax on Net Income of Category E :*

State tax	15.40
Additional taxes	1.10
	<u>16.50</u>

VI. SALARIES AND WAGES.

(a) *Salaries of Private Employees.*

State tax	5.60
Additional taxes	Nil

(b) *Salaries of Public Officials.*

State tax	4.20
Additional taxes	Nil

(c) *Pensions and Salaries of Workmen.*

State tax	1.40
Additional taxes	Nil

VII. LIBERAL PROFESSIONS.

(a) *"Patente" Tax.*

Same tariff as the general "patente" but reduced by 20 per cent.

¹ See "Industrial and Commercial Profits".

	Rate of tax in percentage of the taxable income
(b) <i>Category G Tax on Net Income.</i>	
State tax	15.40
Additional taxes	3.30
	18.70

VIII. COMPLEMENTARY TAX ON TOTAL INCOME.

Income between	Percentage applicable to the slice of income comprised between the two figures of the "Income" column	Amount of tax corresponding to the second figure of the "Income" column
(in drachmæ)		(in drachmæ)
0 and 100,000.	0	—
100,000 and 125,000.	1	250
125,000 and 150,000.	2	750
150,000 and 175,000.	3	1,500
175,000 and 200,000.	4	2,500
200,000 and 230,000.	5	4,000
230,000 and 260,000.	6	5,800
260,000 and 290,000.	7	7,900
290,000 and 320,000.	8	10,300
320,000 and 360,000.	9	13,900
360,000 and 400,000.	10	17,900
400,000 and 440,000.	11	22,300
440,000 and 480,000.	12	27,100
480,000 and 540,000.	13	34,900
540,000 and 600,000.	14	43,300
600,000 and 700,000.	15	58,300
700,000 and 800,000.	16	74,300
800,000 and 1,000,000.	17	108,300
1,000,000 and 1,200,000.	18	144,300
1,200,000 and 1,600,000.	19	220,300
1,600,000 and 2,000,000.	20	300,300
2,000,000 and 2,600,000.	21	426,300
2,600,000 and 3,200,000.	22	558,300
3,200,000 and 4,000,000.	23	742,300
4,000,000 and 5,000,000.	24	982,300
5,000,000 and over	25	—

HUNGARY

BY

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PART I. — GENERAL DESCRIPTION OF DIRECT TAXATION SYSTEM. ¹

The Hungarian system of direct taxation consists of a group of income taxes completed by property tax and of certain imposts (*Gebühren*) which, although not classified in the budget as income taxes, are nevertheless levied upon annual revenue. ²

Individuals and partnerships, on the one hand, and companies on the other, are taxed according to different methods.

As regards the former category of taxpayers (individuals and partnerships), the income taxes are made up of a number of schedular taxes (taxes on income from buildings, landed property, salaries and wages, directors' fees, profits), supplemented by the income tax proper and the property tax.

Companies which are subject, like all taxpayers, to the two taxes on income from landed property and from buildings, are not liable to profits, income or property taxes; instead, they pay a special levy known as "company tax".

Income tax and property tax are progressive, and their rates are fixed with reference to the number of dependents of the taxpayer and his personal circumstances.

The taxes on salaries and wages and on directors' fees are also graduated, but not the taxes on buildings, on land property and on profits.

Company tax is graduated, but the scale of its tariff is based on the rentability of the taxable enterprises.

All the above-mentioned taxes, with the exception of the tax on salaries and wages, are paid directly by the taxpayers themselves.

As already explained, in addition to these taxes there exist imposts on dividends and interests. These charges are paid by the persons who owe the taxable income and withheld by them at the time of paying. The rates are, in principle, proportional.

There are further charges on mining concessions and the extracting industries. They only resemble income tax in that they are payable annually. They will, however, be briefly mentioned in the course of our analysis of the various income taxes and similar imposts.

I. LAND TAX.

Land tax ³ is imposed upon the ground income from land, forests, plantations and other rural estate situated in Hungary.

¹ Legislation in force on June 15th, 1933.

² A few figures will give an idea of the importance in the public revenues of the principal taxes dealt with in the study. The following estimates of receipts are found in the State budget for the fiscal year 1932: Tax on income from landed property, 31,000,000; tax on income from buildings, 87,000,000; company tax, 18,500,000; income tax, 42,000,000; property tax, 16,000,000; special tax on salaries and wages, 24,000,000; tax for the support of the disabled, 8,800,000 pengö.

The total of the above-mentioned taxes represents, therefore, a little less than one-third of the ordinary revenue (direct taxes, excise taxes, registered duties, Customs duties, monopolies, State properties, etc., of the Ministry of Finance.

On the other hand, the taxes on salaries and wages and on profits, which are both at present communal receipts, have been, for the fiscal year 1931, 21,000,000 and 24,000,000 pengö.

³ Laws of 1927, Chapter 100; Laws VII of 1875, V of 1909, IV of 1924 and XXIII of 1929.

It follows from the nature of this tax that the person liable is the person who enjoys the landed income or ground income (*revenu foncier*) — *i.e.*, the owner or usufructuary. The domicile, residence and nationality of the beneficiary are of no importance ; the tax is in every case on the income from real estate situated in Hungary.

The land tax, be it noted, is levied exclusively upon the " ground income " (*revenu foncier*) proper, while income from the development of land and rural property is subject to the same taxes as are imposed upon any independently exercised profit-seeking activity (profits tax or company tax).

The tax is levied upon land entered in the land register as arable land, gardens, meadowland, vineyards, grazing land, forests, etc.

The following land is exempt from this tax : public highways, railways and their appurtenances, built-over land, canals, cemeteries, public gardens, nursery gardens, vine nurseries, artificial ponds.

The following may, on application, be temporarily exempted : land newly planted with trees (for twenty to forty years), new vineyards (for six to ten years) and land newly taken into cultivation (for fifteen years).

The tax is assessed, without the taxpayer's assistance, by the communal authorities on the basis of the particulars of income as they stand in the land register (*cadastre*) on December 31st of the year preceding the tax year.

The income in the register (cadastral income) is net income — *i.e.*, income which, having regard to the region in which the land in question is situated, the form of cultivation and the quality of the soil, represents the average agricultural yield of that land, after deducting ordinary working expenses.

If land becomes unfit for development and on that account exempt from tax, or in the opposite event, or if the form of cultivation has undergone a change, the income in the register may be modified accordingly.

Tax exemption or reduction is allowed in case of acts of God involving total or partial loss of the harvest.

The amount of tax (20 per cent of the net cadastral income) has to be paid to the authorities of the commune in which the taxable estate is situated, in four equal instalments on the first day of each quarter. These payments, however, may be made at any time before the middle of each quarter, without incurring interest charges.

Since the tax is assessed on the basis of the land register, no notice is delivered, unless there is some change of assessment or in the person of the taxpayer.

Should a taxpayer consider that his assessment is unfair, he may appeal to the Royal Office of Contributions within a fortnight of receiving notice of the assessment (*Collected Laws and Decrees*, No. 100 P.M., of 1927, and Law No. XXIII of 1929).

II. TAX ON BUILDINGS.

Like the previous tax, the tax on buildings¹ is levied exclusively upon income from property situated in Hungary, irrespective of the nationality, domicile and residence of the recipient of such income. It differs, however, from land tax in that it is imposed upon the gross income from property and buildings intended for letting.

The tax on buildings is levied upon buildings erected for a period exceeding one year. Floating installations and temporary erections are by their nature not liable to this tax. Further, certain buildings are exempted by reason of their purpose or the status of their owner. This applies to Government buildings, buildings belonging to public corporations, churches and religious edifices,

¹ Laws of 1927, Chapter 200; Laws XXII of 1922, II of 1929, XXIII of 1929 and XXIX of 1929, Ordinances No. 2030 M.E. of 1932 and No. 1390 M.E. of 1933.

educational establishments, premises occupied by the Diplomatic Corps (subject to reciprocity), etc. Buildings and premises used in commerce, industry or agriculture are also exempt.

New buildings enjoy temporary exemption — normally for ten years, but recent legislation has in certain cases extended the period to fifteen, twenty, twenty-five and even thirty years.

For purposes of tax assessment, taxable buildings are divided into those which are let and those which are not let.

The basis of taxation for let buildings is the annual income corresponding to the rent received for the last quarter before the tax year. Rent includes all contributions due from the tenant in cash or in kind, except charges for heating, lighting, etc. In the case of furnished rooms, 30 per cent of the rent is deducted as representing the rent of the furniture.

The taxable sum in the case of unlet buildings is the rental value as determined by comparison with let buildings.

Mortgage interest or other charges upon the building are not deducted from the taxable income or rental value.

Every owner of taxable premises must, during the November preceding the tax year, submit a return of the income he derives to the authorities of the commune in which the property is situated.

The tax is assessed on the basis of this return, duly checked. The rate is 17 per cent at Budapest, 16 per cent in other towns and 14 per cent in the villages. As mentioned above, this rate is calculated on gross income, whereas the 20 per cent land tax is on net income. Taxpayers are informed of the amount of tax due by notices, which are usually delivered during the first two months of the tax year. Payment is made in four equal instalments during the first half of each quarter, interest being charged up to 12 per cent on arrears of payment. If notice for the current year has not been received, taxpayers must pay their instalments on the basis of the previous year's assessment.

The Administration may remit the tax when the taxable building has ceased to yield an income or has been destroyed through an act of God, and also when the owner has been deprived of all or part of his rent by reason of premises being vacant through no act of his or by reason of defaulting tenants. Applications for remission of tax must be submitted to the communal authority within a fortnight of the event justifying remission.

If the taxpayer considers his assessment excessive, he may appeal to the Finance Department within a fortnight of receiving his demand note. Appeal against the Department's decisions lies with the Administrative Tribunal.

EXTRAORDINARY TAX ON BUILDINGS.

This tax was introduced in 1931. Its rate is 5 per cent of the rental value and 20 per cent of the assessed tax on buildings. Exemption is granted in favour of small dwellings occupied by their owners, provided there are not more than two rooms.

III. MINING TAXES.

These imposts are not, strictly speaking, part of the income-tax system ; but, as they are annual contributions due in respect of certain property rights, they may be conveniently dealt with here.

There are two sorts of mining taxes : the tax on coal mines¹ and the tax on quarries, metal and mineral deposits, etc.² Both taxes are purely territorial and are levied exclusively on mining concessions and operations situated in Hungary.

¹ Laws XVII of 1921 and V of 1927.

² Laws XII of 1920 and V of 1927.

The colliery tax is from 16 to 80 filler per annum per acre (arpent) of concession.

Mines other than collieries, quarries and deposits are subject to an annual control duty of 11 pengö ; further, a ground tax of 22 pengö is payable per unit of exploitation ; these units are 45,116 square metres for underground workings and 115,092 square metres for open workings.

Both are assessed by the Royal Captancy of Mines on the basis of the taxpayer's return, and operators or concessionaires are required to pay the amounts due in two equal instalments, on January 1st and July 1st of the tax year, to the Royal Captancy of Mines, within whose jurisdiction the mine or quarry is situated.

IV. TAX ON SALARIES AND WAGES.¹

Any person who has workmen or employees in his service must deduct the amount of this tax from the salaries, wages and other remuneration he pays them.

The tax is thus levied upon all remuneration for work done on behalf and under the direction of another, provided such remuneration is paid in Hungary or corresponds to services rendered in Hungary, and irrespective of the domicile or residence of the beneficiary.

The taxable sum includes, not only cash payments, but any advantages in kind which may accrue to workmen and employees from their employment.

The rate of tax rises from 0.5 to 7.5 per cent for annual remuneration, income below 960 pengö being tax-free. Salaries exceeding 3,000 pengö per month are taxed at 7.5 per cent.

The tax due is normally computed by the employer, who has to pay monthly to the authorities of the commune in which he employs the taxable persons the sums he has withheld for tax from their salaries and wages. The employer must accompany his payments by a list showing the remuneration from which tax has been withheld.

Remuneration paid by a foreign employer is not liable to the tax on salaries if the person concerned can show that, besides income tax, he has to pay in the country whence this remuneration is derived a tax corresponding to the tax on salaries, and that there is a reciprocity agreement between Hungary and that country.

The State has handed over the revenue from the tax on wages and salaries to the communes in order that they may balance their budgets.

SPECIAL TAX ON SALARIES.

In 1930, a special tax on wages and salaries was introduced, the yield of which was to be reserved for the State ; public officials and private employees are alike liable (Law No. XLVII of 1930). Since 1931, however, the latter have had to pay twice as much as the former (Ordinance No. 4740 M.E. of 1931). Salaries and wages not exceeding 120 pengö a month are exempt from this special tax. The tax is withheld by the employer and paid by him to the Treasury. Its yield is estimated in the national budget at 24,000,000 pengö. This tax is now increased by an additional tax of 25 per cent of its amount in favour of the State (Ordinance No. 1390 M.E. of 1933).

V. PROFITS TAX.

1 and 2. TAXPAYERS AND TAXABLE INCOME.

Profits tax¹ is imposed on individuals, partnerships, and limited partnerships. It does not touch share companies or other legal entities assimilated for fiscal purposes to such companies, all of which are liable to company tax in lieu both of profits and income tax.

¹ Laws of 1927, Chapter 300 ; Laws XXIII of 1922 and XXIII of 1929.

All income not subject to land or buildings tax, the tax on salaries and wages, or tax on interest and dividends, is liable to profits tax. It is thus leviable in principle on all income from activities exercised by the recipient independently and on his own behalf, whether the income is the fruit of labour only, of labour combined with capital, or is unearned.

Accordingly, the tax is levied upon the income, profits and other advantages derived from any commercial, industrial, mining, agricultural or forestry enterprise, from any liberal profession and any other profit-seeking activity exercised in Hungary by a person on his own behalf and in his own name. At the same time, even income from some other source is liable to profits tax if by its nature (patent and copyright royalties) it cannot be made liable to one or other of the taxes enumerated in the preceding paragraph. The same applies to annuities which persons living in Hungary derive from abroad.

The profits of branches or subsidiaries abroad are only exempt from the tax if the taxpayer can show that he pays abroad, in addition to income tax, a tax corresponding to the Hungarian profits tax and that there is reciprocity of treatment between Hungary and the foreign country.

Persons domiciled abroad and not resident in Hungary will be liable to the tax only if they carry on their industry, trade or profession in Hungary.

Further, if persons domiciled abroad merely buy goods or raw materials in Hungary for consignment to their foreign warehouses, these purchases are not liable to profits tax. Finally, the Minister of Finance is empowered to grant fiscal exemption (subject to reciprocity) to foreign artists and lecturers visiting Hungary professionally.

3. ASSESSMENT OF TAX.

RETURNS.

Taxpayers must file the return for this tax during February of the tax year to the authorities of the commune in which they exercise their profession or have their industry or trade or in which the tax is assessed. If they possess establishments in several communes, they must make a separate return in each, for tax will in this case be computed separately for each establishment.

The return must indicate the net profit remaining after subtracting from gross receipts all the deductions which the law allows.

The returns are checked by the authorities, who may ask for oral or written explanations from the taxpayer concerned, examine his books and accounts, summon witnesses and institute an expert enquiry.

Should the taxpayer's accounts not be considered satisfactory, or if the information and other data he furnishes are insufficient, the Administration may assess his income by such external evidence as rent, staff, material, motor-cars, domestic servants, personal expenditure, etc.

The same applies when the taxpayer furnishes no declaration or submits it after the prescribed time-limit.

COMPUTATION OF TAXABLE INCOME.

The tax is based on the net income for the year preceding the tax year. The net income is the difference between gross income and the total cost of acquiring and maintaining that income.

The following are included among deductible costs :

1. Cost of purchasing raw materials ; operating and administrative costs, cost of upkeep of material, plant and buildings used in the enterprise ; wages, salaries and rents.

2. Annual depreciation of premises not liable to the tax on buildings and depreciation of plant, material and furniture used in the enterprise.

In order, however, that these forms of redemption may be deducted, they must appear in the balance-sheet and profit-and-loss account accompanying the return.

3. Operating losses for the previous year and bad debts, if included in the balance-sheet.

4. Contributions actually paid to Chambers of Commerce, insurance premiums, direct taxes or indirect contributions paid by the enterprise to the State or communes. Death duties and Customs duties may not be deducted, nor may profits tax.

5. Interest on debts and other liabilities incurred in connection with industrial or commercial operations. Interest on other debts may not be deducted.

6. During the first year of business, initial expenses, but not capital expenditure and purchases of equipment, etc.

The above-mentioned costs may not be deducted from income when the latter has been determined empirically — *e.g.*, on the basis of turnover or from certain external signs, since these forms of assessment give the net income direct.

When the same taxpayer owns several enterprises, he is not allowed to deduct from the income of one expenses or losses in connection with others.

Further, the following may not be deducted from gross income :

1. Expenditure on enlarging the enterprise, increasing its capital or redeeming debt ; also the cost of acquiring new material, except current replacements ;

2. Interest on capital invested in the enterprise by the owner himself or members of his family and the remuneration of his own work or that of members of his family ;

3. Profits tax and, generally, direct State taxes and their supplements ;

4. Gifts and presents, except tips and New Year boxes ;

5. Interest on securities, bills and debts included in the portfolio of the enterprise.

An increase or reduction of the capital invested in the enterprise does not affect the fixing of the taxable net income.

The inventory must in all cases be based on purchase or cost prices. This excludes the possibility of showing an appreciated value as a receipt or a depreciated value as a loss.

COMPUTATION OF TAX.

Once the net taxable profit is determined, the tax is computed. The rate is proportional (5 per cent of income) and there are no basic abatements. The yield accrues to the commune and, if the needs of the latter require it, the Minister of Finance may raise the rate to 10 per cent.

4. COLLECTION OF TAX.

Notices are issued by the Administration in May, and payment is made under the same conditions and at the same dates as income tax.

VI. COMPANY TAX.¹

1 and 2. TAXPAYERS AND TAXABLE INCOME.

Company tax is payable by :

1. Share companies, partnerships with share capital, mining companies and co-operatives ;

¹ Laws of 1927, Chapter 400 ; Laws XXIV of 1922 and of 1927 and Ordinance No. 1390 of 1933.

2. Industrial and commercial enterprises belonging to the State or to other public corporations ;

3. Tramways, local railways and savings banks.

As already mentioned, these corporations and enterprises are liable to neither income tax nor profits tax.

Company tax is levied upon all income accruing to the taxable company, even income liable to some other tax (such as land and buildings taxes) ; in the latter case, the income liable to company tax is reduced by the amount on which the other tax was computed and paid.

Hungarian companies — that is, companies incorporated in Hungary — which have their head office in the country and are duly registered in the Commercial Register there, are taxable both in respect of the profits and income they receive in Hungary and in respect of those they derive from abroad.

Foreign companies, on the other hand, are only liable to company tax in respect of profits and income they derive from operations carried on or property owned in Hungary.

3. ASSESSMENT OF TAX.

RETURNS.

Companies liable to this tax must submit to the Royal Administration of Taxes annually, within four months of closing their accounts, a return of income accompanied by the balance-sheet, profit-and-loss account, report of the board of managers and minutes of the general meeting relating to the allocation of profits and the distributions of dividends and directors' fees.

This return must indicate the profits of the last business period accounted for. If this period is more or less than twelve months, the profits figure will be increased or reduced so as to correspond to the length of that period. In the case of new enterprises, tax is not assessed until the first balance-sheet has been drawn up, and this balance-sheet serves as the basis of taxation for the first and second years of the enterprise's existence.

COMPUTATION OF TAXABLE INCOME.

The law prescribes that the tax shall be computed on the basis of declarations and balance-sheets ; it invests the fiscal authorities with powers of investigation in the matter both of income tax and profits tax and lays down definite rules concerning the sums that should be deducted from, and added to, profits as shown in the balance-sheet, before tax is computed.

1. The following items should, according to circumstances, be added to profits or deducted from expenses :

(a) Losses brought forward from previous years, except in respect of the year immediately preceding ;

(b) Property tax, any charge or impost, other than direct taxes and turnover tax, paid or payable by the enterprise itself, and also any tax or charge paid on behalf of others — *e.g.*, employees, creditors, shareholders, etc. ;

(c) Gifts, donations and other free contributions, except those made for religious purposes or to educational institutions, as well as New Year presents and other gifts made in the interests of the enterprise ;

(d) Initial expenditure (new enterprises, however, may deduct these costs from their profits for the first year, and share companies may make the deduction for five years) ;

(e) Depreciation of property subject to land tax ;

(f) New purchases which cannot be regarded as contributing to the maintenance or completion of the stock and equipment of the enterprise ;

(g) Sums devoted to increasing the company's capital and enlarging the enterprise ;

(h) Sums devoted to repayment of loans or redemption of capital, except in the case of an enterprise whose exploitation or property must, under a concession contract, revert after a number of years to the State, a public corporation or some other body or person ;

(i) In the case of an enterprise with establishments in several countries, the sums paid by the Hungarian establishment to the head office or establishment abroad as interest on, or repayment of, capital, or as its share in the general expenses of the foreign establishment or head office (this provision does not apply to regular current account operations for which the rate of interest is normal, or when the share of general expenses imputed to the Hungarian establishment is in proportion to the gross receipts) ;

(j) Advantages in cash or kind accruing to the founders of share companies and sums devoted to the repurchase of their shares ;

(k) Interest paid to shareholders ;

(l) Reserves other than those which by law may be deducted from profits ;

(m) The difference between the figures at which the company's securities stand in the balance-sheets of the previous year and the tax year respectively, when the latter figure is below the latest rate quoted for these securities on the Budapest Exchange during the tax year or, if not quoted, below the market value of these securities (if the securities have been bought during the tax year itself, an addition will be made to profits when the figure at which they are entered in the balance-sheet is both less than the purchase price and less than the last rate quoted on the Exchange or than the actual market value) ;

(n) The difference between the figures at which material and inventory stand in the balance-sheets of the previous year and tax year respectively, when the latter figure does not correspond to the market value of the property in question. The same additions will be made to profits when material and stocks bought during the tax year are entered in the balance-sheet at a value below the purchase price and more than 20 per cent below their market value ;

(o) Generally, any profit resulting from the accounts, even if not entered as such therein.

2. The following are not to be included among taxable profits and must therefore be deducted from the profits shown in the balance-sheet :

(a) Grants and subsidies to employees of the enterprise, insurance institutions, pensions and to relief funds, if the latter are legally distinct from the enterprise ; this provision applies both to voluntary and free grants and to those compulsory by law ;

(b) Sums placed by insurance companies to premium reserves, to other technical reserves and to cover casualties notified but not yet settled, and shares in the profits ascribed to holders of life insurance policies ;

(c) Sums set aside by any enterprise as allowances for the depreciation of the premises, equipment, machinery, installation and tools used in its operations. The amount of depreciation allowance is a question depending upon the nature and use of the goods. In practice, however, the tendency is to allow 2 per cent and 7.5 per cent for the normal depreciation of real and personal property respectively. Should the Administration be in doubt as to how much to allow, it may order an expert enquiry, in which case the enterprise may employ a counter-expert of its own ;

(d) Sums placed to reserve by enterprises holding a concession, for the amortisation of

property which, on the expiry of the concession, will cease to belong to the enterprise and become the property of the conceding party ;

(e) Sums placed to reserve during the lifetime of a patent, to amortise its value ;

(f) Sums set aside to cover bad or doubtful debts ;

(g) Profits brought forward from previous years ;

(h) In the case of mining concerns, 2 per cent of the purchase price paid to the landowners for the definitive concession of the right to work the deposit annually until the successive deductions amount to the purchase price ;

(i) As regards consumers' co-operatives, the refund paid to members out of surplus profits, in proportion to their purchases ;

(j) Sums employed from reserves already taxed ;

(k) Directors' percentages and staff bonuses, on condition that these payments are liable respectively to the tax on directors' percentages and the tax on salaries and wages ;

(l) Sums received over and above the nominal value of new shares issued by a share company ; but interest paid by the subscribers to these shares cannot be included among these sums (such interest is normally demanded when the new shares are issued during the business year and the dividend payable on these new shares will be based upon the total profits of the current year) ;

(m) The amount by which the price for which foreign works or factories were sold exceeds the value ascribed to these works in the previous year's balance-sheet, provided that this excess has not been distributed wholly or in part among the members of the company. The same rule applies to the amounts by which the selling price of a company's foreign share holdings exceeded the value at which these shares were entered in the balance-sheet of the previous year ; the company must, however, have in its portfolio, at the time of sale, at least 25 per cent of the foreign company's shares, or the shares must represent the value of an enterprise situated abroad which has been sold by the company. The company has to inform the Finance Minister of all such sums not appearing in the balance-sheet when it makes its return.

Such are the items which the law expressly excludes from taxable profits. If, however, sums are used for a purpose other than that which justified their being excluded from taxable profits, they will become liable to tax like any other profits. This happens when deductible reserves are used to increase the capital or are distributed as surplus capital when a company is dissolved. Further, the law allows the Minister of Finance, if the public interest demands it, to authorise enterprises to build up tax-free reserves, provided that the purpose of these reserves is clearly defined.

Accordingly, the taxable amount is made up of profits as shown in the balance-sheet, plus any additions or minus any deductions prescribed by law.

The authorities responsible for assessing the tax have the right to examine the profit-and-loss account and check whether the sums paid to members of the Board and the staff are in proportion to the nature and size of the enterprise. If they are not, any unjustified difference must be added to the taxable sum.

In the case of a Hungarian branch of a foreign company, special attention is paid to the prices at which raw materials or goods supplied by the foreign enterprise are invoiced to its Hungarian establishment. If these prices appear abnormal, the assessing authority may adjust them — if necessary with the aid of experts ; the enterprise is free to employ a counter-expert at its own expense.

COMPUTATION OF TAX.

The rate of tax differs according to the taxpayer's status.

In the case of share companies, partnerships with share capital, mining companies, railways,

savings banks and financial establishments, the rate varies with the profit-making capacity of the enterprise — *i.e.*, according to the proportion between profits and the enterprise's capital proper. By "capital proper" is meant paid-up capital plus reserves made up of profits already taxed.

No reserve built up without being taxed can be regarded as belonging to capital proper. The premium is on issue of capital-stock and insurance reserve against accidents are part of capital proper, but life insurance reserves are not.

The tax rises on a sliding scale from 16 per cent for enterprises whose profits represent 10 per cent of their capital to 30 per cent for enterprises whose profits exceed 40 per cent of the capital.

Co-operative societies whose distributed profits do not exceed 6 per cent of their capital pay at the rate of 10 per cent; others at the rate applicable to share companies and companies assimilated thereto.

Enterprises owned by the State or by public corporations are not taxed on their profit-earning capacity, but on a sliding scale fixed according to the actual amount of their profits, the rate varying between 5 per cent for profits not exceeding 6,000 pengö and 15 per cent for profits in excess of 60,000 pengö.

With a view to increasing fiscal revenue, it has been decided that, as from 1932, company tax is to be collected even from companies whose balance-sheet shows no net profit; in these cases the rate is fixed at 2 per thousand of the capital. It should be added that since 1933, the company tax is increased by a supplementary tax of 40 per cent of its amount (Ordinance No. 1390 M.E. of 1933).

Once the tax is assessed, the tax office sends the company a demand note. If the company wishes to appeal, it must do so to the Finance Department within a fortnight of receiving the note. Appeal against the decisions of the Department may be lodged with the Administrative Tribunal during the fortnight following their notification (*Collected Laws*, No. 400 of 1927).

4. COLLECTION OF TAX.

The tax is payable quarterly, the first instalment being due on January 1st. But, as declarations need not reach the Administration till April, owing to the fact that they need not be made until four months after the close of the accounts, and since the Administration delivers the notices between July and September, payments due before receipt of notice are made on the basis of the tax paid the year before, and settlement takes place at the end of the year, if the amount due for that year differs from that of the previous year.

VII. TAX ON DIRECTORS' PERCENTAGES.

Share companies and other legal entities liable to company tax must further pay the tax on directors' percentages¹ in respect of the share of profits they allow to their directors, auditors and other members of their management.

In order that the tax may be payable, there must be a distribution of directors' fees. That is to say, the sums paid must not be in the nature of salaries for work done on the company's behalf, but must be due by reason of the recipient's status and paid out of the company's profits.

This tax, being withheld from the fees distributed, is levied upon the recipients of these fees, but the domicile and residence of the beneficiary are of no importance from the fiscal standpoint and, in order that directors' percentages may be taxable, the company or corporation distributing them need only be liable to company tax. In the case of a foreign company, the portion of its directors' fees that will be taxable is calculated in the same way as the profits on which it is liable to company tax.

On the other hand, when persons domiciled in Hungary receive directors' percentages from foreign companies not liable to company tax, they will not be held liable to the tax on directors' percentages.

¹ Laws of 1927, Chapter 400, Laws XXIV of 1922 and V of 1927.

The rate of tax is 16 per cent for distributions not exceeding 3,000 pengő, 20 per cent for sums between 3,000 and 10,000 pengő, and 28 per cent for higher sums.

Companies which have to withhold the tax must declare to the Royal Administration of Finance the percentages which it has been decided to pay, within four months of closing their accounts. This declaration is made at the same time as that of the profits on which company tax is payable. The tax on directors' percentages is paid in four equal instalments at the beginning of each quarter.

SPECIAL TAX ON DIRECTORS' PERCENTAGES.

Article 1 of Ordinance No. 4740 M.E. of 1932 establishes a special tax on directors' percentages, the rate being the same as that of the special tax on salaries and wages and having likewise been increased by 25 per cent under Article 6 of Ordinance No. 1390 M.E. of 1933.

VIII. TAX ON DIVIDENDS.

The tax on dividends,¹ as its name implies, is imposed upon the profits which share companies and other companies liable to company tax distribute to their shareholders. It is levied, not only on declared dividends, but also on profits distributed in the form of capital surplus when companies are dissolved, or distributed in the form of new shares when a company's capital is increased (without any payment by shareholders) out of reserved profits.

The rules governing liability to dividends tax of dividends paid to persons domiciled or resident abroad or by companies whose head office is abroad, are the same, *mutatis mutandis*, as those applicable to the tax on directors' percentages.

The rate is 0.5 per cent of the gross sums or advantages distributed.

Companies must declare to the authorities the amount of dividend the general meeting has decided to distribute, at the same time that they make their return for purposes of company tax.

The tax is paid to the fiscal authorities by the company, which withholds the tax when paying the dividends to their recipients (Article 16 of Law XXIV of 1930 and Article 27 of Law V of 1927).

IX. TAX ON INTEREST.

The tax on interest² is, in principle, leviable on :

1. Income from bonds and similar securities issued by the State, public corporations and enterprises which are required to publish their accounts and which have their head office in Hungary ;

2. Interest from investments with financial institutions, savings banks, co-operative societies, bankers and exchange agents, whether these investments are placed to current account, on deposit or otherwise ;

3. Interest which a taxpayer other than a bank, co-operative society or savings bank receives from his debtor in respect of money lent (Ordinance No. 1820 M.E. 1932).

The tax is due irrespective of the creditor's domicile or residence.

The rate of tax is normally 10 per cent, but is reduced to 5 per cent for railway company loans.

The Minister of Finance has further exercised his legal right to reduce or remit the tax payable on investments in Hungary by individuals or enterprises having their domicile or head office abroad, in so far and for as long as the public interest may dictate, by exempting from the tax interest on securities held by foreigners and on funds invested in Hungary.

¹ Laws of 1927, Chapter 400 ; Laws XXIV of 1922 and V of 1927.

² Laws of 1924 ; Ordinance No. 3700 of 1926 of the Minister of Finance.

In cases 1 and 2, those who owe interest and coupons liable to the tax must declare the same within a fortnight of their falling due, and must pay the tax within six months of that date. They may, and must, withhold tax from the interest they pay ; the tax is thus deducted at the source.

The creditors mentioned in No. 3 have themselves to pay the tax on the interest they receive within a week.

X. INCOME TAX.

Individuals, partnerships, limited partnerships and estates (including estates in abeyance, estates in bankruptcy and sequestrated property) are liable to income tax,¹ which is in the nature of a complementary tax imposed upon income already subject to some other tax.

1 and 2. TAXPAYERS AND TAXABLE INCOME.

The extent of liability depends upon whether the taxpayer is or is not domiciled or resident in Hungary ; if he is, he is liable, not only on income arising in the country, but on income derived from abroad, subject to the reservations contained in double-taxation conventions.

Foreigners who reside in Hungary for at least one continuous year are similarly liable to tax in respect of all their income, whether derived from Hungary or from abroad. Others, however, are only liable to this tax in respect of income obtained or paid to them in Hungary.

Thus, Hungarians living abroad have to pay income tax on income derived from Hungary, and, therefore, on the income from capital invested in Hungary or from a mortgage loan secured on real estate in Hungary. On the other hand, foreigners living abroad are not liable on income from these sources, but they have to pay tax on income derived from other Hungarian sources.

For purposes of applying these principles, domicile is understood as the place where a person lives or stays in circumstances that imply an intention to make more than a temporary stay there.

The following is income in respect of which persons subject to a limited fiscal liability are liable to income tax :

1. Rent from real estate situated in Hungary, which has already paid the tax on land or buildings ;
2. Interest or income from mortgage debts secured on real estate situated in Hungary, which has already been held liable to the tax on interest ; but foreigners living abroad are, as already mentioned, not liable to tax on this form of income ;
3. Profit from agricultural and forestry enterprises situated in Hungary ;
4. Profits from Hungarian branches of industrial, mining and commercial enterprises ;
5. Income from liberal or other professions carried on in Hungary.

The three last-mentioned classes of income are all liable to the profits tax before being liable to income tax.

6. Salaries, wages and pensions corresponding to some present or past work performed in Hungary or paid by the State or public corporations (this income has already been subject to the tax on salaries and wages) ;

7. Dividends, directors' percentages, interest and other income from shares, bonds and other securities issued by public corporations, and companies having their head office in Hungary. Foreigners living abroad are not subject to tax on this kind of income.

Dividends have already been taxed indirectly through company tax and the tax on dividends ; directors' percentages have paid company tax and the tax on directors' fees, while interest on bonds and other securities has paid the interest tax.

8. Profits from the sale of real estate situated in Hungary.

¹ Laws of 1927, Chapter 500 ; Laws X of 1903, XLVI of 1914, XXVI of 1916, IX of 1918, XXIII of 1920, XXXIII of 1923, V of 1927, XXIII of 1929 and Ordinance No. 1390 M.E. of 1933.

EXEMPTIONS.

The following income is always free of income tax :

- (a) Total incomes not exceeding 1,000 pengö a year and incomes in excess of 1,000 pengö, when their taxable part does not exceed 600 pengö ;
- (b) Parliamentary salaries ;
- (c) Pensions paid by a taxpayer voluntarily to relatives (ascendant, descendant or collateral) ;
- (d) Allowances to disabled persons ;
- (e) Army pay ;
- (f) Salaries of civil servants ;
- (g) Remuneration of private employees amounting to less than 3,600 pengö a year.

3. ASSESSMENT OF TAX.

RETURNS.

Persons liable to income tax must make a return of their income to the authorities of the commune in which they are domiciled, in February of the tax year. Persons not resident in the country must make their return at the place where the source of income is situated.

The returns are checked by the Administration, which may correct them after hearing the taxpayer and collecting all evidence and witnesses' statements which it may see fit to obtain.

If the taxpayer fails to furnish his return within the prescribed time-limit, or to supply the evidence asked for by the Administration, the latter may assess the tax *ex officio* on the basis of external evidence or by comparison with taxpayers in a similar situation.

COMPUTATION OF TAXABLE INCOME.

The taxable income is the total net income of each class enjoyed by the taxpayer during the previous calendar year, except in the case of income derived from a profession, trade or industry for which the taxpayer keeps accounts extending over a period not corresponding to the calendar year.

In this latter case, tax is assessed on the results of the business year ending during the preceding calendar year.

The incomes of members of one family living in the same home must be added together, and the tax, computed on this total, must be paid by the head of the family. But members of the family whose taxable income exceeds 600 pengö are taxed separately.

Income to be taken into account for purposes of determining the taxable sum may be classified as follows :

1. Income from agricultural and forestry concerns ;
2. Income from, or rental value of, land and buildings ;
3. Income from trade, industry, mining and any other business liable to profits tax .
4. Income from capital ;
5. Remuneration of personal services ;
6. All other income not included in any of the foregoing groups.

From the gross amount of this income must be deducted :

- (a) All expenses incurred in acquiring, insuring and maintaining the income, including the cost of the upkeep, replacement and use of property serving to produce the income ; also rent and insurance premiums ;
- (b) Cost of the upkeep and repair of buildings and charges and other expense which the use of the buildings entails, unless such expenses are borne by the taxpayer ;
- (c) Operating losses on the business year preceding the tax year, provided the taxpayer can furnish evidence of his income by a profit-and-loss account made out in due form.

From the total income thus established are deducted all dues and taxes paid by the taxpayer during the tax year. These include :

- (a) All direct taxes on behalf of the State, municipalities and communes, and parish contributions ;
- (b) Indirect State and communal taxes, turnover taxes, taxes and fees on agreements and other instruments, incurred in the course of the operations from which the income was obtained ;
- (c) Contributions to chambers of commerce and other professional organisations.

Interest paid by the taxpayer on legally established debts is also deducted from total income. There is no occasion to deduct the above charges when the income has been determined empirically, as that method has already taken account of such charges.

Nor is it permissible to deduct expenditure in the form of gifts, expenses incurred in adding to the property, debt redemption and household expenditure.

If part of the total income is tax-free, income tax is, of course, fixed without regard to such part. Tax-free income is only taken into account to ascertain whether the total income exceeds the taxable minimum and whether, therefore, the person concerned is taxable or not.

If the taxpayer can show that, as regards his income from abroad, he already pays income tax or a similar tax in the foreign country, that income will not be taxed, granted reciprocity of treatment.

COMPUTATION OF TAX.

Taxpayers whose total income does not exceed 1,000 pengö are exempt. Those, however, who do not possess income to this amount in Hungary, but whose total income, including income from abroad, is more than 1,000 pengö, are liable if their Hungarian income amounts to 600 pengö or more.

The tax is graduated on two separate scales. The first is applied to legal entities, minors, clergymen and taxpayers who have more than two dependents. This, the ordinary scale, rises from 1 per cent to 40 per cent, the latter rate being imposed on income above 1,200,000 pengö.

Taxpayers with incomes below 6,000 pengö benefit by a reduction of tax according to the number of their dependents.

The higher scale is applied to all taxpayers not entitled to benefit by the ordinary scale ; it rises from 1.284 per cent to 44 per cent.

4. COLLECTION OF TAX.

The tax is paid quarterly, the first instalment being due on January 1st, but each payment may be made at any time during the first half of the quarter without interest being charged. Notices are sent out in May of the tax year and payments due before receipt of the notice are made

on the basis of the tax paid the year before, and, if the amount due for the current year is different from that of the preceding year, the difference is deducted from, or added to, payments made after the notice has been received.

ADDITIONAL INCOME TAX.

Since 1932, income tax has been increased by an addition equal to 30 per cent of its amount (Ordinance No. 2030 M.E. 1932). Since January 1st, 1933, the rate of this additional tax has been raised to 60 per cent of the income tax (Ordinance No. 1390 M.E. of 1933).

XI. PROPERTY TAX.

The property tax¹ supplements the income tax, and its purpose is to increase the fiscal burden on income from permanent sources.

The close connection between property tax and income tax is emphasised by the fact that both these personal taxes are assessed simultaneously and by the same rules.

I. TAXPAYERS.

Property tax is levied upon individuals, landed estates in joint-ownership, foundations, estates in abeyance, estates in bankruptcy and sequestered property.

Nationals permanently resident in Hungary, or, though not continuously resident in the country, having premises fitted up there for permanent residence, are liable to property tax, not only on their property situated in Hungary, but on personal property situated abroad. On the other hand, nationals permanently residing abroad are only liable on their property in Hungary.

Foreigners are liable under the same conditions as nationals. There are, however, these two exceptions :

1. Foreigners who, although not permanently domiciled in Hungary, live there for at least one continuous year, must pay property tax ;

2. Foreigners not domiciled on Hungarian territory and not living there for a continuous period of one year are not liable to property tax in respect of their capital invested in Hungary.

In cases of usufruct, the usufructuary and not the owner is taxed.

2. TAXABLE PROPERTY.

Tangible property situated outside Hungarian territory is never regarded as taxable and is left out of account for purposes of tax assessment. Capital invested abroad is taxable if it belongs to persons domiciled in Hungary or resident there for at least a year. It escapes the tax, however, if the owner can show that it is liable abroad to a property or similar tax and that there is a convention granting reciprocity in fiscal matters between the foreign country concerned and Hungary.

Property tax is imposed on the following property : real estate with all its parts and appurtenances and rights attaching thereto ; the assets of an agricultural or forestry concern ; the assets of an industrial, commercial or any other profit-seeking enterprise ; capital ; all other personal property.

The following are not regarded as property liable to the tax : household furniture, clothing, linen, works of art, books, household utensils and such articles as cannot be classed in any of the above groups.

¹ Laws of 1927, Chapter 500 ; Laws XXXII of 1926, IX of 1928, XXIII of 1920, V of 1927, XXIII of 1929 and Ordinance No. 1390 M.E. of 1933.

3. ASSESSMENT OF TAX.

DETERMINATION OF TAXABLE AMOUNT.

Returns and the methods of taxation follow the same rules as apply to income tax.

Property and its various elements are assessed according to the situation on the last day of the year preceding the tax year.

The only exception to this rule is in the case of an enterprise whose business year does not coincide with the calendar year. In this event, the return and assessment are based on the data obtaining on the last day of the business year. This exception, however, is only allowed if the books of the enterprise are properly kept and if the accounts are closed after September 30th.

To the property of the head of a family must be added the property of all the members of the family whose incomes, according to the rules governing income tax, form part of the income of the head of the family.

The various elements of which property is composed having been assessed and added together, the result is the taxable sum, from which must be deducted :

- (a) The taxpayer's debts ;
- (b) Twenty times the amount of pensions and other payments incumbent upon him.

COMPUTATION OF TAX.

Personal exemption from property tax is granted to persons whose property does not exceed 5,000 pengö or, if their income is free of income tax, 25,000 pengö in value.

The property tax is on a sliding scale from 0.1 to 1 per cent. The latter rate is levied on property of a net value of more than 19,000,000 pengö.

4. COLLECTION OF TAX.

Property tax is collected under the same conditions and at the same times as income tax.

SPECIAL PROPERTY TAX.

Beginning with 1932, a special property tax is to be levied, the rate being 100 per cent of the ordinary property tax.

XII. TAX FOR THE SUPPORT OF THE DISABLED.

The yield of the tax on behalf of disabled ex-service men¹ is specially intended to cover part of the cost to the State of pensions for disabled ex-service men and for the widows and orphans of men who fell in the war. This tax is a separate levy and it is supplementary, on a gently sliding scale, to the taxes on land and buildings, companies, directors' percentages, profits and income. The highest rate is 5 per cent and is applicable when the total of the principal tax exceeds 240 pengö a year.

¹ Laws of 1927, Chapter 700 ; Laws XLVIII of 1925, V of 1927 and Ordinance No. 1390 M.E. of 1933.

PART II.—TAXATION OF FOREIGN AND NATIONAL ENTERPRISES.

A. FOREIGN ENTERPRISES.

1. DEFINITION AND GENERAL PRINCIPLES.

In Hungary, a foreign enterprise, for fiscal purposes, is any enterprise which belongs to individuals or companies having their domicile or head office abroad. These enterprises are accordingly liable only in respect of income and profits they derive from Hungary. They are taxed on the whole of those profits, by means either of the income and profits taxes or of company tax (see remarks on these two taxes in Part I). They may also be liable to the land and buildings tax, the taxes on interest and dividends and to other direct taxes, if they are in receipt of income which is by its nature subject to one or other of these taxes.

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) DIVIDENDS.

Dividends paid by Hungarian companies or other legal entities to foreign enterprises are liable to deduction of dividends tax at source in the same way as are dividends paid to national enterprises. Further, the enterprise to which these dividends are paid must declare them and itself pay either income and profits tax or company tax, to whichever it is itself liable.

(b) INTEREST.

I. *On Bonds.*

In principle, the interest and coupons of bonds, mortgage loans and other fixed income securities issued by the State, public corporations and companies having their head office in Hungary, are liable to deduction at source of interest tax at 10 per cent. All such income, however, if accruing to persons domiciled or having their head office abroad, is exempt from this tax by a decree of the Minister of Finance. It continues, however, to be liable to other taxes, and foreign enterprises will further be subject in respect of this interest to either income tax or company tax.

2. *On Secured Loans.*

Loans secured on real estate situated in Hungary are also liable to the tax on interest. The rate is reduced to 5 per cent for coupons of mortgage bonds. The Minister of Finance may further grant temporary exemption to this interest, and in the exercise of this right he issued Decree No. 30000 of 1927.

3. *On Unsecured Loans.*

Interest on sums lent to individuals is subject to the tax on interest and also liable to income and profits tax or to company tax.

(c) DIRECTORS' PERCENTAGES.

Directors' percentages distributed by Hungarian companies to persons domiciled or resident abroad are liable to the tax on directors' percentages in the same way as those distributed to persons living or having their head office in Hungary. These percentages will also be liable to income tax.

(d) ROYALTIES FOR USE OF PATENTS, COPYRIGHTS, TRADE-MARKS, SECRET PROCESSES AND FORMULÆ AND SIMILAR INCOME.

Royalties and income from the sale or lease of patents registered in Hungary, artistic, literary copyrights, or industrial property rights are liable to the tax on profits and income tax or to company tax, according to the status of the person or enterprise in receipt of such income.

(e) RENTS FROM REAL ESTATE, MINING ROYALTIES AND SIMILAR INCOME.

Income from real estate in Hungary is liable, whatever the owner's status, to land tax or to the tax on buildings ; it is also liable to company tax or income tax if the owner or the usufructuary is personally liable to one of these taxes. Further, in the case of land or buildings belonging to an enterprise liable either to profits tax or company tax, the portion of income from such property that has not been imposed by one of these two property taxes is included among the total taxable profits liable either to profits tax or to company tax.

Income derived from the lease of a business, or industrial establishment or from the lease of mining or other concessions is liable either to the tax on profits or to company tax.

(f) GAIN DERIVED FROM THE PURCHASE AND SALE OF REAL ESTATE, SECURITIES AND PERSONAL PROPERTY.

If an industrial or commercial enterprise derives profit from the purchase or sale of personal or real property, such gains, even if occasional, must be included among profits liable either to company tax or to the tax on profits. If the operations are conducted by individuals who have no industrial or commercial organisation and do not habitually engage in these transactions, only the profits from the sale of real estate are taxable. Moreover, such purchase and sale must have been made for a purpose of gain, which intention is assumed when sale followed purchase within less than five years. In this case, however, the taxpayer is allowed to show proof that the property sold was not acquired with a view to its resale.

(g) SALARIES, WAGES, COMMISSIONS AND OTHER REMUNERATION FOR SERVICES.

If the remuneration is for the work of an employee — that is, work done on behalf and under the direction of another — it is liable to the tax on salaries and wages. This tax is deducted at source and is imposed on all salaries and wages paid in return for services rendered in Hungary, whatever the domicile or residence of the beneficiaries. The emoluments of the liberal and other independently exercised professions are liable to the tax on profits, which is payable if the profession or occupation from which the income is derived is carried on in Hungary.

(h) INCOME FROM A TRUST.

Trusts, as understood in Anglo-Saxon law, do not exist in Hungary.

(i) INCOME FROM CARRYING ON BUSINESS OR INDUSTRY.

1. *Through Local Commission Agent or Broker.*

Foreign enterprises which have no place of business in Hungary, but only buy or sell there through commission agents or brokers, are not taxed.

2. *Through a Local Dealer or Distributor.*

The same is the case when the foreign enterprise delivers its products to retail dealers and tradesmen who buy and resell them, even if these dealers have an exclusive right to retail the goods bought, or some other privilege.

3. *Through a Travelling Salesman, whether or not having Power to conclude a Contract.*

When a foreign enterprise employs a commercial traveller to visit Hungary and to solicit and take orders there, there is, in principle, no fiscal liability. But if the commercial traveller is the exclusive representative of the enterprise and operates permanently in Hungary or on any part of Hungarian territory, the foreign enterprise is regarded as being represented in Hungary and is on that account liable to tax.

4. *Through a Local Agent with a Power of Attorney.*

If a foreign enterprise has entrusted its representation to an agent established in Hungary, who is empowered to conclude operations in its name, the foreign enterprise is held to be liable.

5. *Through an Agent selling out of a Stock belonging to the Foreign Enterprise.*

Again the foreign enterprise is liable.

6. *Through a Permanent Establishment of Any Kind.*

The term "establishment" includes factories, workshops, agencies, depôts, offices, shops and representatives used to further the activities which the enterprise pursues. The term also includes premises which the enterprise may own, even if it does not use or exploit them directly, but lets them to third parties.

If a foreign enterprise is regarded as possessing an establishment in Hungary, it is liable either to income tax and tax on profits, or to company tax, in the same way and to the same extent as was explained with reference to each of these taxes in Part I.

B. NATIONAL ENTERPRISES.

Hungarian fiscal law regards as national all enterprises which belong to individuals domiciled in Hungary or to companies having their centre of management there. These enterprises are, according to their nature, liable in respect of all their income, derived from both foreign (unless a convention granting reciprocity in fiscal matters has been concluded between Hungary and the respective foreign country) and Hungarian sources, to income and profits taxes or to company tax. They are not, however, liable to the taxes on land and buildings, or the taxes on dividends, directors' fees and interest, in respect of income they derive from real or personal property, tangible and intangible, situated abroad. In the case, moreover, of enterprises with real property or establishments abroad, the income from such property or establishments is exempt from the taxes on income, profits and companies, if it is liable to a special tax abroad and if the country whence the income is derived grants reciprocal exemption to income from Hungarian sources, either in virtue of its own municipal legislation or under treaties.

If foreign income is taxable, the tax is assessed and computed under the same conditions and at the same time as the tax on the whole taxable income.

C. DOUBLE-TAXATION AGREEMENTS.

The Kingdom of Hungary has concluded double-taxation agreements with Czechoslovakia, Germany, Austria, Italy, Yugoslavia and Roumania ¹.

These agreements introduce certain exceptions to the rules of domestic law set forth in the two preceding chapters of this part of the study.

Before explaining the scope of these exceptions as regards the taxation of the chief kinds of income dealt with above, a few general remarks must be made concerning the effects of these agreements upon income tax and property tax.

Under the agreements, the right to levy income tax on the rents, interest, profits, etc., from real estate, secured and unsecured loans, industrial and commercial enterprises, and services (including remuneration from the public funds) is subject to the same rules as are applied to the various real or personal taxes upon each of these kinds of income, referred to above. Income tax on all other income — *viz.*, dividends, directors' percentages, annuities, interest on bonds, interest on bank deposits, etc. — is imposed only in the country where the recipient of the income is domiciled.

The right to levy property tax is subject to the same rules that govern the collection of income tax.

DIVIDENDS.

Dividends are liable to the real taxes in the State in which the company that pays them is domiciled; but the right to impose these dividends under income tax belongs to the State in which the creditor is domiciled.

INTEREST.

Bond interest is taxed according to the same rules as dividends.

As regards interest on bank *deposits*, *current accounts* and savings bank deposits, the position is as follows:

Impersonal tax is imposed in the State in which the debtor is domiciled, personal tax in that of the creditor's domicile. The Conventions, however, prescribe that, if an enterprise which receives sums on deposit or for current account has establishments in several States, impersonal tax is collected by the State in which is situated the establishment directly in receipt of these deposits or sums.

The Conventions with Poland, Yugoslavia and Roumania stipulate that interest on *unsecured loans* between individuals shall be liable to impersonal tax in the State where the debtor is domiciled and to income tax in the State where the creditor is domiciled. The Conventions with Austria, Germany, Czechoslovakia and Italy, however, decide that this interest shall be taxable only in the State in which the recipient of the interest resides.

Income from *loans secured by mortgage* and similar loans is liable to impersonal taxes in the State where the real property is situated and to income tax in the State where the creditor is domiciled.

DIRECTORS' PERCENTAGES.

Under the Conventions concluded with Czechoslovakia and Austria, the right to impose impersonal tax on directors' percentages belongs to the State in which the company distributing them has its head office.

In the Convention with Germany, this right is ascribed to the State in which the enterprise has its real centre of management.

The Conventions with Italy and Yugoslavia lay down that, if the company distributing directors' percentages has its head office in one State and its centre of management in the other, the supreme financial authorities of the two States shall agree in each particular case upon an equitable basis for the allocation of tax.

¹ Translations of these Conventions are contained in the volume "Double Taxation and Fiscal Evasion" (document C.45. M.110), published by the League of Nations in 1928, except that of the Convention with Roumania, which was concluded in 1932.

The Convention with Poland has decided that the right to impose impersonal tax belongs to the State in which the company has its head office, unless the enterprise's real centre of management is in the other State.

The right to collect income tax is reserved in any case to the State in which the recipient of the directors' percentage is domiciled.

ROYALTIES FOR USE OF PATENTS, COPYRIGHTS, TRADE-MARKS, ETC., AND ANNUITY INTEREST.

Royalties for use of patents and other income from incorporeal property rights, also life annuities, are taxable only in the State in which the beneficiary is domiciled.

RENTS FROM REAL ESTATE, MINING ROYALTIES AND SIMILAR INCOME.

Income from real estate is liable to land and buildings tax in the State in which the property is situated. Income tax, too, is levied in this State and not in the State in which the beneficiary is domiciled. Further, if taxpayers are liable in the State of their domicile to company tax, this tax is not imposed upon that part of taxable profits which represents the yield of property situated in another State.

SALARIES, WAGES, COMMISSIONS AND OTHER REMUNERATION FOR SERVICES.

All the agreements, except that with Roumania, stipulate that wages and salaries are taxable in the country in which the work they correspond to was accomplished.

Pensions paid by private enterprises are taxed in the State where the beneficiary is domiciled.

The Convention with Roumania decides that taxation rests with the State in which salaries, wages and pensions are paid. Income from personal services — *i.e.*, from the liberal professions — is liable to tax in the country in which the services are performed.

There are, however, special provisions to meet the case of foreign artists and *savants* who work abroad in a temporary capacity : under Conventions concluded with Czechoslovakia, Germany, Austria and Poland, such persons are not liable to tax in the country where they are staying merely temporarily. The Conventions with Yugoslavia and Roumania contain no such provision, with the result that the fees paid to artists and *savants* for temporary work abroad are liable in the country where the work is done, both to the special taxes and to income tax.

INCOME FROM A BUSINESS OR INDUSTRY.

All the agreements concluded by Hungary stipulate that the profits from industrial or commercial activities of any kind whatever are liable to the special taxes on these profits and to income tax only in the State in whose territory the enterprise has an establishment, even if the operations of the enterprise extend to another country. The Conventions add that the profits taxable in the State where there is an establishment are the profits ascribable to that establishment.

Nevertheless, the provisions relating to Danube shipping enterprises are based on a different principle : the right to impose tax belongs exclusively to the State in which the enterprise has its head office.

The agreements with Italy and Poland define what is to be understood by "establishment". This term includes all permanent installations in which an enterprise conducts all or some of its operations. In particular, the following are establishments of an enterprise : its head office, its real centre of management, its branches, factories, workshops, offices of purchase or sale, shops, warehouses and any other industrial and commercial installation in which the owner of the enterprise, his responsible agents or other representatives can carry on the activities for which the enterprise exists. Further, any permanent representation of an enterprise in a particular country is to be regarded as an establishment.

PART III. — METHODS OF ALLOCATING TAXABLE INCOME.

A. FOREIGN ENTERPRISES WITH LOCAL BRANCHES OR SUBSIDIARIES.

I. GENERAL QUESTIONS AND METHODS OF APPORTIONMENT.

(a) BOOK-KEEPING AND ACCOUNTING REQUIREMENTS.

Hungarian fiscal law lays down no special rule as to how industrial and commercial enterprises shall keep their books and accounts, and enterprises, both foreign and national, have only to keep the books prescribed by commercial legislation. These are :

(1) The day-book, in which must be entered in order of date all operations effected, all expenditure and all receipts of the enterprise in question ;

(2) The inventory, which must be drawn up once on commencing business and subsequently at the close of each fiscal year. It must contain details of all real and personal property, debts constituting the enterprise's assets and the various items included among liabilities.

All traders are required to keep copies of outgoing, and originals of incoming, correspondence for ten years.

Further, share companies, partnerships with share capital, mining and assimilated companies have to publish an annual balance-sheet in the form of a classified list of assets and liabilities as they stand at the close of the fiscal year.

But although fiscal law does not, strictly speaking, prescribe the keeping of books and accounts in any special manner, it does impose certain requirements as to what shall constitute the profits to be shown in the balance-sheet and the liabilities to be deducted therefrom. These provisions were indicated under the heading " Assessment of Tax " in the passage on profits and company taxes in Part I.

(b) METHODS OF ALLOCATION.

The problem of allocating income only arises in connection with income tax proper and the company and profits taxes. The land and buildings taxes, the tax on salaries and wages and those on directors' fees, dividends and interest are levied only on income from property situated in Hungary or from operations conducted exclusively in that country. Hungarian law does not expressly regulate the allocation of profits, and the only legal provisions governing the matter are contained in conventions for the avoidance of double taxation which Hungary has concluded with her neighbours. Apart, however, from the cases covered by international conventions, administrative practice adopts the following rules and methods of procedure.

I. *Method of Separate Accounting.*

Since enterprises and companies liable to profits and income taxes or to company tax are taxed on the basis of their accounts as shown in the balance-sheet attached to their declaration, it follows that foreign enterprises are only taxable in respect of their profits. As regards foreign

enterprises which are liable only in respect of their Hungarian establishments, assessment will be based on the accounts of those establishments, but the law prescribes that these enterprises shall attach, to their statement of the results of their establishments, the general balance-sheet of the whole enterprise. A comparison of these two balance-sheets very often leads to corrections being made on the balance-sheet of the Hungarian establishment. Comparison of the two documents and examination of the accounts of the Hungarian establishment very often show that taxation based on the balance-sheet or accounts leaves certain profits of the Hungarian establishment out of the reckoning. In this case, the method of separate accounting is discarded, and recourse is had to one of the methods described below.

The same applies when the accounts of the establishment are found to be incomplete or even not to exist.

2. *Method of Fractional Apportionment.*

If the tax cannot be assessed with reasonable accuracy on the basis of the separate accounts, the fiscal authorities employ the method of fractional apportionment. In the case of commercial establishments the profits assessable against the Hungarian establishment are determined by ascribing to that establishment that share of the enterprise's total net profits which corresponds to the ratio between the gross receipts of the establishment and the gross receipts of the enterprise as a whole.

In the case of insurance companies, allocation will be based, not on the ratio between gross receipts, but on the relation between premiums paid in Hungary and premiums paid abroad.

As regards other enterprises, the apportionment fraction is the ratio between salaries and wages paid in Hungary and those paid abroad.

Frequently, however, this method, like that of separate accounting, is inapplicable. The reason for this, as a rule, is that it is impossible to secure exact data showing the gross receipts of the enterprise's foreign establishments.

3. *Empirical Methods.*

If it is impossible to determine the income of Hungarian establishments either on the basis of their own accounts or by comparison with the total results of the whole enterprise, the Treasury has recourse to estimates, based either on a comparison with Hungarian enterprises of a similar kind or on certain external evidence.

The factors used for purposes of comparison are as a rule the amount of capital, fixed, working and floating.

The external evidence is found in the rental value of the premises used by the enterprise, the size of the plant, the number of employees and the size of the pay-roll.

4. *Requirements for Selection of Methods and Value of the Various Methods.*

As already mentioned, the Administration is under no legal obligation to observe any special order of preference in its choice between the different methods of allocation. In practice, however, the method first tried is that of separate accounting, and only if the results appear unconvincing is recourse had to methods of fractional apportionment.

An empirical method is only used in the last resort, when other methods have failed.

(c) APPORTIONMENT BETWEEN BRANCH AND PARENT ENTERPRISE.

1. *Apportionment of Gross Profit of Local Branch to Real Centre of Management abroad.*

Under Hungarian fiscal law, by which all the profits realised in Hungary are taxable, it is the rule that no part of the profits of the Hungarian branch may be ascribed to the real centre of

management abroad. Nevertheless, under fractional apportionment, and if profits are assessed with reference to the total profits of the whole enterprise, they may be indirectly so ascribed.‡

2. *Apportionment of Expenses of Real Centre of Management to Branch.*

The fiscal law of Hungary has no definite rules for allocating the interest charges and general overhead of foreign enterprises.

The tendency in practice, however, is to admit that, when a debt has been incurred in the general interest of the enterprise — *i.e.*, when the Hungarian establishment has profited from borrowed capital along with other parts of the enterprise, part of the interest on this debt may be deducted from the profits of the Hungarian establishment. The same is true of general overhead corresponding to expenditure which has been useful, not only to the foreign establishments, but to the establishment in Hungary.

This portion of debt interest and general overhead is ascribed to the Hungarian establishment whether the latter is assessed by the method of separate accounting or by the method of fractional apportionment. If, however, the taxable profits are assessed empirically, this apportionment is not allowed.

3. *Apportionment of Net Profit of Branch to Deficitary Enterprise and vice versa.*

Tax being assessed exclusively on the results of the Hungarian establishment, the fact that the whole enterprise operates at a loss is of no account for fiscal purposes.

This rule can be applied without any difficulty if the Hungarian establishment can be taxed on the basis of its separate accounts. But if, in such case, this method cannot be employed, recourse will be had, not to fractional apportionment, under which losses of the whole enterprise would reduce the taxable profits of the Hungarian establishment, but rather to empirical methods.

If the accounts of the Hungarian branch show a loss, while the whole enterprise operates at a profit, the Hungarian establishment will still be liable. In such case, empirical methods or the method of fractional apportionment will be used, and not the method of separate accounting.

(d) APPORTIONMENT BETWEEN PARENT ENTERPRISE AND SUBSIDIARIES.

In some circumstances, the Treasury may consider that an enterprise, although constituted as a Hungarian company with its head office in Hungary, is under the dominant control of a foreign enterprise, and that all the activities of the company in Hungary are directed towards furthering the interests of the enterprise on which it is dependent. In such case, the Administration assimilates the subsidiary company to a mere branch or to an establishment having no independent legal entity, and the methods and rules of allocation applying to branches proper are extended to these subsidiary companies.

II. APPLICATION OF THE METHODS OF ALLOCATION IN SPECIFIC CASES.

(a) INDUSTRIAL AND COMMERCIAL ENTERPRISES.

I. *Selling Establishments.*

Local Establishments selling in National Markets.

Establishments which enterprises maintain in Hungary for the sale of goods or products they have manufactured abroad are liable to Hungarian tax. The profits of these establishments are

usually assessed on the basis of separate accounting, but administrative practice has established no definite rules for the apportionment of profits as between the sales branch and the purchase and manufacturing branches.

Nevertheless, the balance-sheet of a Hungarian branch of the foreign enterprise is always checked to see how raw materials and goods have been invoiced by the foreign enterprise to its establishment in Hungary. It is the duty of the Administration to examine the books of the Hungarian establishment, if necessary with expert aid, in order to determine the cause of losses or insufficient profits. If these are due to the invoiced prices, the Administration corrects the latter on the basis of cost prices or the actual purchase prices of the foreign enterprise.

Local Establishments of Foreign Enterprises selling abroad.

If a foreign enterprise has a branch in Hungary which sells in a foreign country, where the enterprise has no establishment, the income taxable in Hungary will include the profits from these sales.

2 and 3. *Manufacturing and Processing Establishments.*

If a foreign enterprise has workshops, factories or other installations in Hungary, where it manufactures or processes goods for export and sale abroad, it will be held taxable in respect of the industrial and manufacturing operations it conducts in Hungary. If, as very often happens, the accounts of the Hungarian establishment do not show these industrial profits, the Administration, assisted if necessary by an expert, checks the invoiced prices and makes any necessary corrections. Otherwise, and especially for the assessment of profits tax (not therefore company tax), they are determined either empirically or by the method of fractional apportionment, account being taken of the ratio between salaries and wages paid in Hungary and those paid abroad.

4. *Buying Establishments.*

If a foreign enterprise buys goods in Hungary for sale abroad, it is not taxable unless it has a permanent establishment or agency within the country. If it is so taxable, the profits are assessed by the method best suited to the particular case.

5. *Research or Statistical Establishments, Display Rooms, etc.*

As a rule, the existence of an establishment justifies liability to tax in Hungary. But as Hungarian fiscal law aims at taxing the commercial profit only, the authorities do not, in practice, tax establishments such as research or statistical offices which earn no direct profits. The same applies to display rooms where no contract is concluded. If contracts are concluded, the establishment will of course be taxable, and tax will be assessed by the methods ordinarily used for establishments of foreign enterprises.

(b) OTHER KINDS OF ENTERPRISE.

No special allocation problems normally arise for enterprises other than industrial or commercial. It may be mentioned, however, that the profits of banks and credit institutions are usually determined on the basis of separate accounts. So are those of insurance companies, unless their balance-sheets are inexact or ambiguous, in which case profits are taxed on the basis of the ratio between premiums received in Hungary and total premiums received in all countries.

The few railways not owned by the State are also taxed on the basis of their balance-sheets. Similarly, in the case of other transport enterprises, power, light and gas, and mining enterprises, the method of separate accounting is preferred. If recourse is had to fractional apportionment, allocation is based on the ratio between salaries and wages paid in Hungary and those paid abroad.

No question of allocation arises in connection with telephone and telegraph enterprises, which are a Government monopoly.

B. NATIONAL ENTERPRISES WITH BRANCHES OR SUBSIDIARIES ABROAD.

The profits of national enterprises are allocated according to their origin, when there is occasion to claim an exemption in respect of the profits of their foreign establishments or from property situated abroad.

These profits are exempt from profits and company taxes when the foreign country imposes upon them a direct tax similar to the Hungarian tax on the same profits and when the foreign country does not tax the profits of the Hungarian establishments of its own national enterprises.

If profits are allocated according to their origin, the same methods are employed, *mutatis mutandis*, as are used for foreign enterprises with establishments in Hungary.

C. TRUST AND HOLDING COMPANIES.

I. NATIONAL HOLDING COMPANY CONTROLLING ONE OR MORE FOREIGN SUBSIDIARIES.

Even if a Hungarian company holds part of the capital of a foreign company, so that the latter is controlled and governed by the Hungarian company, there is no departure from ordinary law : the profits of the branch will not be taxable in themselves, and the dividends and advantages accruing to the holding company will be liable to company tax in the same way as its other profits.

II. LOCAL SUBSIDIARY COMPANY CONTROLLED BY A FOREIGN HOLDING COMPANY.

When a foreign holding company holds shares in a Hungarian company, but without thereby acquiring control over the latter, the fiscal position will be the same as that of all other companies whose capital is divided among the shareholders — *i.e.*, the Hungarian company will be liable to company tax and will withhold from the dividends and directors' fees it pays to the foreign company the tax on these two classes of income.

The case is different when the foreign company holds such a large part of the Hungarian company's capital that the latter becomes economically subject to the foreign enterprise. In this event, the remarks made under the heading "Apportionment between Parent Enterprise and Subsidiaries" will apply.

D. DOUBLE-TAXATION AGREEMENTS.

According to the different double-taxation conventions, if an enterprise has establishments in both contracting States, tax may only be levied in each State on the income from business transacted by an establishment situated in that State.

Further, the Conventions with Italy and Poland formally emphasise that, with a view to allocating the income between the two contracting States, the financial authorities of each State may request taxpayers to submit statements of their general and special accounts and any other documents provided for by the law of the respective States. Should it be impossible to employ

such documents, the supreme financial authorities of the two contracting States shall agree upon the measures to be taken to secure a fair and equitable apportionment of income.

The Convention with Czechoslovakia does not classify the head office of an enterprise among establishments ; in the other Conventions, the head office or real centre of management is so included.

The detailed rules for allocating the income of profit-seeking enterprises between the two States have been fixed in relations with Austria, through a special agreement concluded on November 8th, 1924, which contains the following clauses :

“ 1. In assessing, for taxation, the sales office of a producing undertaking situated in the other State, the taxable business profits in respect of the sales office shall be reckoned at one-third of these total profits accruing from the sales effected through the said office. Where the sales office also undertakes purchases, its quota shall be raised to one-half. Where purchases are effected by a branch situated in the one State, and sales by an establishment situated in the other State, the total profits accruing from such business transactions shall be allocated in equal parts. Profits which accrue from the joint activities of the two branches and which are to be allocated between the two States shall be reckoned on the total profits of the undertaking in accordance with the ratio of the turnover resulting from such joint activities and the total turnover of the undertaking. Where profits are obtained exclusively owing to the activities of one of the two business establishments, they shall be reckoned on the total profits in accordance with the ratio of the turnover resulting from such activities and the total turnover of the undertaking. In no case shall the quota falling to the State in which is situated the centre of management (either alone or together with other business establishments) of an undertaking liable to company tax be less than one-tenth of the total profits. The fiscal authorities of the two States may jointly effect the allocation on the basis of the closed accounts, where it seems probable that any such division will not differ appreciably from the probable results of applying the aforementioned principles of division.

“ 2. In the calculations provided for in the foregoing paragraph, turnover expressed in different currencies shall be reckoned according to the average rate quoted on the Vienna Exchange (mean cheque rate on Budapest) during the period for which the taxes are payable. The average will be calculated according to the rates on the 1st, 11th and 21st of each month of the period in question. In the event of no quotation being made on one of the specified days, the first quotation given after this day shall be taken. Both parties agree that profits expressed in different currencies should be converted at the rate of the day on which the balance-sheet was drawn up.

“ 3. Where a branch, in cases other than those already mentioned, engages in business transactions on behalf of a branch situated in the territory of the other State, the customary commission shall be regarded as profits in the State in which the transactions in question were effected.

“ 4. If the results obtained by the application of the foregoing principles are obviously at variance with the actual profits earned, the two financial administrations may agree upon another method of allocation.

“ 5. In the case of branches of credit institutions, the profits of the branch shall be deemed to be the portion of the total profits of the undertaking which corresponds to the ratio of the costs for staff borne by the branch and the costs for staff borne by the undertaking as a whole. In the case of branches of insurance companies, the allocation shall be effected in accordance with the ratio of the premiums dealt with by the branch establishment of the insurance company and the total premiums received by the undertaking.

The Conventions which Hungary has concluded with States concerned in river traffic on the Danube (Germany, Austria, Czechoslovakia, Yugoslavia and Roumania) lay down as a fundamental principle that shipping enterprises on the Danube shall be liable to taxes on their business income only in the State in which they have their head office.

Under the special agreement concluded with Austria, a railway company whose head office is in one of the two States and whose operations extend into the territory of the other State is liable to industrial and commercial profits tax only in the State where it has its head office, unless it operates a section of line in the other State which is longer than fifteen kilometres ; if it is, the enterprise will be taxed in the two States in proportion to its operations in each (paragraph 3, Article 3, of the Treaty). The agreement also provides that, at the request of either of the two Administrations, the items on which assessment is to be based shall be apportioned in any particular case by special agreement.

Annex.

TARIFF OF DIRECT AND ASSIMILATED TAXES.

I. TAX ON LANDED PROPERTY. ¹

20 per cent of the cadastral net income.

II. TAX ON BUILDINGS. ²

17 per cent in Budapest
 16 per cent in other cities } of gross income.
 14 per cent in villages

III. TAX ON PROFITS. ³

5 per cent of net income. ⁴

IV. COMPANY TAX. ⁵

1. Share companies, partnerships with share capital, limited liability companies, mining companies, co-operative societies with profits exceeding 6 per cent of their capital, railways, savings banks and financial institutions :

16%	if the profits do not exceed 10%	of the company's capital.
18%	if the profits represent 10-15%	of the company's capital.
20%	if the profits represent 15-20%	of the company's capital.
22%	if the profits represent 20-25%	of the company's capital.
24%	if the profits represent 25-30%	of the company's capital.
26%	if the profits represent 30-35%	of the company's capital.
28%	if the profits represent 35-40%	of the company's capital.
30%	if the profits exceed 40%	of the company's capital.

¹ Article 1 of the Law XXIII, of 1929.

² Article 1 of the Law II, of 1929.

³ Article 17 of the Collected Laws No. 300 and of Executive Regulation No. 30000, of 1927.

⁴ The rate of tax accruing to communes may, by a decision of the Finance Minister, be doubled.

⁵ Article 19 of the Collected Laws No. 400 and of Executive Regulation No. 40000, of 1927.

2. State enterprises and public corporations :

Amount of Profits	Rate of Tax Percentage
Not exceeding 6,000 pengö	5
From 6,000-12,000 pengö	6
From 12,000-18,000 pengö	7
From 18,000-24,000 pengö	8
From 24,000-36,000 pengö	9
From 36,000-48,000 pengö	10
From 48,000-60,000 pengö	12
Above 60,000 pengö	15

Company tax is increased by an additional tax equal to 40 per cent of its amount (Ordinance No. 1390 M.E. of 1933).

V. TAX ON DIRECTORS' PERCENTAGES. ¹

Taxable Amount	Rate of Tax Percentage
Not exceeding 3,000 pengö	16
Between 3,000 and 10,000 pengö	20
Over 10,000 pengö	25

Directors' percentages are, in addition, liable to a special tax on directors' percentages whose tariff is the same as that of the special tax on salaries and wages ² and has been likewise increased by 25 per cent (Ordinance No. 1390 M.E. of 1933).

VI. TAX ON DIVIDENDS. ³

0.5 per cent of the dividends.

VII. TAX ON INTEREST. ⁴

10 per cent of the taxable income.

¹ Article 19 of Collected Laws No. 400 and of Executive Regulation No. 40000, of 1927.

² Article 1 of the Ordinance No 4740, of 1931 and Ordinance No. 1390 M.E. of 1933.

³ Article 27 of the Law V, of 1927.

⁴ Article 1 of the Ordinance No. 3700 P.M., of 1926, and of the Ordinance No. 1820, of 1932.

VIII. TAX ON SALARIES AND WAGES. ¹

AMOUNT OF TAXABLE INCOME (In pengő)		AMOUNT OF TAX (In pengő)		
		Tax corresponding to the amount of income equal to the "income" column	Amount of tax corresponding to the part of income exceeding the first figure of the "income" column (to be calculated by slices)	
Between	And			Amount of the slices
1. Salaries exceeding 20 pengő per week :				
20	45	0.10	5	0.05
45	95	0.30	5	0.10
95	145	1.30	5	0.15
145	150	2.80	5	0.20
150	170	3	10	0.25
170	320	3.50	10	0.50
320	360	11	10	1
360	405	15	15	1
405	450	18	15	1.50
450	525	22.50	25	2.50
525	650	30	25	3
650	700	45	50	5
700	750	50	50	6
2. Salaries exceeding 80 pengő per month :				
80	180	0.40	20	0.20
180	380	1.60	20	0.40
380	580	5.20	20	0.60
580	600	11.20	20	0.80
600	680	12	40	1
680	1,280	14	40	2
1,280	1,440	44	40	4
1,440	1,620	64	60	4
1,620	1,800	72	60	6
1,800	2,100	90	100	10
2,100	2,600	120	100	12
2,600	2,800	180	200	20
2,800	3,000	200	200	24
3,000	and above	224	200	15

¹ Article 18 of the Finance Ministry Ordinance No. 300, of 1927.

IX. SPECIAL TAX ON SALARIES AND WAGES. ¹

Note. Under Ordinance No. 1390 M.E. of 1933, the rates below should be increased by 25 per cent.

AMOUNT OF TAXABLE INCOME (In pengő)		AMOUNT OF TAX (In pengő)			
		Tax corresponding to the amount of income equal to the " income " column	Amount of tax corresponding to the part of income exceeding the first figure of the " income " column (to be calculated by slices)		
Between	And			Amount of the slices	Amount of tax corresponding to each slice or part of slice ²
1. Salaries exceeding 30 pengő per week :					
30	35	0.40	—	—	
35	45	0.40	5	0.10	
45	95	0.60	5	0.20	
95	145	2.60	5	0.30	
145	150	5.60	5	0.40	
150	170	6	10	0.50	
170	320	7	10	1	
320	360	22	10	2	
360	405	30	15	2	
405	450	36	15	3	
450	525	45	25	5	
525	650	60	25	6	
650	900	90	50	10	
900	1,700	140	100	20	
1,700	2,500	300	100	25	
2. Salaries exceeding 120 pengő per month :					
120	140	1.60	—	—	
140	180	1.60	20	0.40	
180	380	2.40	20	0.80	
380	580	10.40	20	1.20	
580	600	22.40	20	1.60	
600	680	24	40	2	
680	1,280	28	40	4	
1,280	1,440	88	40	8	
1,440	1,620	128	60	8	
1,620	1,800	144	60	12	
1,800	2,100	180	100	20	
2,100	2,600	240	100	24	
2,600	3,600	360	200	40	
3,000	6,800	560	400	80	
6,800	10,000	1,200	400	100	

¹ Ordinance No. 4740 M.E., of 1931.

² Figures of this column should be reduced by half in the case of public officials.

3. Salaries exceeding 10,000 pengö per month :

20 per cent of the taxable amount in the case of taxpayers other than public officials.
10 per cent in the case of public officials.

X. INCOME TAX. ¹

I. Normal Rate.

AMOUNT OF TAXABLE INCOME (In pengö)		AMOUNT OF TAX (In pengö)		
		Amount of tax corresponding to the amount of income equal to the first figure of the " income " column	Amount of tax corresponding to the part of income exceeding the first figure of the " income " column (to be calculated by slices)	
Between	And		Amount of the slices	Amount of tax corresponding to each slice or part of slice
(a) Income not exceeding 360,000 pengö :				
600	700	7	—	—
700	1,200	7	100	1
1,200	2,300	12	100	2
2,300	3,500	34	100	3
3,500	4,000	70	100	5
4,000	4,800	95	200	6
4,800	5,200	118	200	7
5,200	6,400	132	200	8
6,400	11,200	180	200	10
11,200	12,000	420	200	15
12,000	17,400	480	300	20
17,400	18,000	840	300	30
18,000	20,000	900	400	40
20,000	23,000	1,100	500	40
23,000	27,000	1,340	500	50
27,000	34,000	1,740	500	60
34,000	35,000	2,580	500	70
35,000	36,000	2,720	500	80
36,000	49,000	2,880	1,000	120
49,000	60,000	4,460	1,000	140
60,000	75,000	6,000	1,000	160
75,000	76,000	8,700	1,000	260
76,000	82,000	8,960	2,000	280
82,000	96,000	9,800	2,000	400
96,000	100,000	12,480	2,000	500

¹ Article 22 of the Collected Laws No. 500, of 1927.

AMOUNT OF TAXABLE INCOME (In pengö)		AMOUNT OF TAX (In pengö)		
		Amount of tax corresponding to the amount of income equal to the first figure of the "income" column	Amount of tax corresponding to the part of income exceeding the first figure of the "income" column (to be calculated by slices)	
Between	And			Amount of the slices
<i>(a) Income not exceeding 360,000 pengö (continued) :</i>				
100,000	105,000	13,480	2,500	500
105,000	107,500	14,480	2,500	520
107,500	120,000	15,000	2,500	600
120,000	140,000	18,000	5,000	2,000
140,000	180,000	26,000	10,000	2,500
180,000	210,000	36,000	10,000	2,700
210,000	220,000	41,100	10,000	2,800
220,000	230,000	47,000	10,000	2,900
230,000	240,000	49,800	10,000	3,000
240,000	280,000	52,800	20,000	5,800
280,000	320,000	64,400	20,000	6,600
320,000	360,000	76,800	20,000	6,600

(b) Income exceeding 360,000 pengö :

Amount of tax corresponding to the part of income which does not exceed 360,000 pengö 90,000 pengö.

Amount of tax corresponding to the part of income which exceeds 360,000 pengö :

AMOUNT OF TAXABLE INCOME (In pengö)		SLICES OF INCOME (In pengö)	RATE APPLICABLE TO EACH SLICE (In pengö)
Between	And		
360,000	380,000	20,000	25.5
380,000	400,000	20,000	26
400,000	425,000	25,000	26.5
425,000	450,000	25,000	27
450,000	475,000	25,000	27.5
475,000	500,000	25,000	28
500,000	525,000	25,000	28.5
525,000	550,000	25,000	29
550,000	575,000	25,000	29.5
575,000	600,000	25,000	30
600,000	625,000	25,000	30.5
625,000	650,000	25,000	31
650,000	675,000	25,000	31.5
675,000	700,000	25,000	32
700,000	725,000	25,000	32.5
725,000	750,000	25,000	33
750,000	775,000	25,000	33.5
775,000	800,000	25,000	34
800,000	825,000	25,000	34.5
825,000	850,000	25,000	35
850,000	875,000	25,000	35.5
875,000	900,000	25,000	36
900,000	925,000	25,000	36.5
925,000	950,000	25,000	37
950,000	975,000	25,000	37.5
975,000	1,000,000	25,000	38
1,000,000	1,050,000	50,000	38.5
1,050,000	1,100,000	50,000	39
1,100,000	1,200,000	100,000	39.5
1,200,000	above		40

2. *Increased Rate.*

The increased rate varies according to the amount of the normal tax, but it is always approximately 10 per cent higher than the normal rate.

3. *Additional Tax.*¹

60 per cent of the basic amount.

¹ Article 3 of the Ordinance No. 1390, of 1933.

XI. PROPERTY TAX. ¹

I. Ordinary Tax.

AMOUNT OF TAXABLE PROPERTY (In pengő)		AMOUNT OF TAX (In pengő)		
		Amount of tax corresponding to the amount of property equal to the first figure of the " property " column	Amount of tax corresponding to the part of property exceeding the first figure of the " property " column (to be calculated by slices)	
Between	And			Amount of the slices
5,000	10,000	6	1,000	1
10,000	20,000	10	2,000	2
20,000	40,000	20	4,000	4
40,000	120,000	40	5,000	5
120,000	180,000	120	5,000	6
180,000	220,000	196	5,000	8
220,000	230,000	244	10,000	9
230,000	240,000	253	10,000	13
240,000	400,000	266	10,000	14
400,000	415,000	490	15,000	14
415,000	460,000	504	15,000	16
460,000	475,000	552	15,000	18
475,000	535,000	570	15,000	20
535,000	955,000	650	15,000	25
955,000	970,000	1,350	15,000	30
970,000	1,000,000	1,380	15,000	40
1,000,000	1,100,000	1,460	25,000	40
1,100,000	1,125,000	1,620	25,000	50
1,125,000	1,175,000	1,670	25,000	55
1,175,000	1,825,000	1,780	25,000	60
1,825,000	2,000,000	3,340	25,000	80
2,000,000	2,300,000	3,900	25,000	100
2,300,000	2,800,000	4,500	50,000	150
2,800,000	3,300,000	6,000	50,000	160
3,300,000	3,850,000	7,600	50,000	180
3,850,000	5,200,000	9,400	50,000	200
5,200,000	6,850,000	15,000	50,000	300
6,850,000	7,050,000	24,600	50,000	400

¹ Article 41, Collected Laws No. 500, of 1927.

² The amount of tax relating to a fraction of slice may never exceed 1 per cent of such a fraction. For example, let us take a property amounting to 8,658,000 pengő ; it is decomposed as follows : 8,475,000 pengő, to which corresponds a tax of 34,000 pengő, plus two slices of 75,000 pengő, on each of which a tax of 500 pengő is due, plus a fraction of slice of 33,000 pengő. For this fraction of slice, the tax may not be of 500 pengő, but will be reduced to 330 pengő — i.e., 1 per cent of 33,000 pengő.

AMOUNT OF TAXABLE PROPERTY (In pengő)		AMOUNT OF TAX (In pengő)		
		Amount of tax corresponding to the amount of property equal to the first figure of the "property" column	Amount of tax corresponding to the part of property exceeding the first figure of the "property" column (to be calculated by slices)	
Between	And		Amount of the slices	Amount of tax corresponding to each slice or part of slice
7,050,000	8,475,000	26,400	75,000	400
8,475,000	9,900,000	34,000	75,000	500
9,900,000	10,800,000	43,500	100,000	500
10,800,000	12,000,000	48,000	100,000	1,000
12,000,000	12,750,000	60,000	150,000	1,000
12,750,000	13,050,000	65,000	150,000	1,500
13,050,000	14,400,000	68,000	150,000	2,000
14,400,000	15,000,000	86,000	150,000	3,000
15,000,000	15,500,000	98,000	250,000	3,000
15,500,000	17,000,000	104,000	250,000	4,000
17,000,000	17,500,000	136,000	250,000	6,000
17,500,000	18,000,000	154,000	250,000	8,000
18,000,000	18,500,000	162,000	500,000	8,000
18,500,000	19,000,000	170,000	500,000	15,000
19,000,000	20,000,000	185,000	1,000,000	15,000
20,000,000	above	200,000	100,000	1,000

2. Additional Tax on Property.¹

The rate of the additional tax on property is equal to 100 per cent of the normal tax on property.

¹ Article 12 of the Ordinance No. 2030, of 1932, and Article 4 of the Ordinance No. 1390, of 1933.

XII. TAX FOR THE SUPPORT OF DISABLED. ¹

Note. Under Ordinance No. 1390 M.E. of 1933 the rates below should be doubled.

I. Rate of the Tax for the Support of Disabled when it is levied on the Basis of Taxes Other than the Tax on Salaries and Wages.
(In pengö.)

Amount of the basic tax	Amount corresponding to the basic tax corresponding to the first figure of the "amount of tax" column	Amount corresponding to the part of tax exceeding the first figure of the "tax" column (to be calculated by slice)	
		Amount of the slices	Amount of tax corresponding to each slice
0-10	0.10	—	—
10-30	0.10	10	0.10
30-40	0.30	10	0.15
40-70	0.45	10	0.20
70-90	1	10	0.30
90-160	1.60	10	0.50
160-200	5	10	1
200-240	9	10	2

2. When the Tax is computed on the Basis of the Tax on Salaries and Wages.

(a) In the case of the tax on salaries and wages being payable weekly :

Amount of the basic tax (in pengö)	Amount of the tax for the support of disabled (in pengö) per week
Not exceeding 2	0.02
Between 2 and 3	0.05
Between 3 and 4	0.10
Between 4 and 5	0.15
Over 5	0.04 (for each pengö or fraction of pengö)

(b) In the case of the tax on salaries and wages being payable monthly :

Amount of the basic tax (in pengö)	Amount of the tax for the support of disabled (in pengö) per month
Not exceeding 8	0.10
Between 8 and 12	0.20
Between 12 and 16	0.40
Between 16 and 20	0.60 (for each slice of 5 pengö or fraction of slice)

¹ Article 5 of the Collected Laws No. 700, of 1927. The tax for the support of disabled is assessed on the basis of the total amount of the taxes on land, on buildings, on companies, on directors' percentages, on salaries and wages, on income and on property, which the taxpayers must pay during the taxable year.

ITALY

BY

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PART I. — GENERAL DESCRIPTION OF INCOME-TAX SYSTEM. ¹

In Italy, the income-tax system is based upon a distinction between impersonal taxes and personal taxes.

Taxes are regarded as impersonal when they are payable simply because the income exists (is produced, that is to say) in Italy, and entirely irrespective of the person who receives it, or of the status and circumstances of such person. "Personal" taxes are taxes for the enforcement of which the law defines the status and taxable capacity of the taxpayer in the light of circumstances attaching to his person.

The following are impersonal taxes :

- (a) The tax on land ;
- (b) The tax on buildings ;
- (c) The tax on income from movable wealth ;
- (d) The tax on agricultural income regarded as movable wealth.

The following are personal taxes :

- (e) The complementary graduated tax on total income ;
- (f) The tax on bachelors of Italian nationality.

I. LAND-TAX.

1 and 2. TAXPAYERS AND TAXABLE INCOME.

The land tax ² is imposed on income that the owner derives from rural property. Income is regarded as derived from landed estate (*reddito dominicale*) when it is obtained from the natural productivity of the land or from capital permanently invested in it.

The tax is leviable on rural estates *situated in Italy*, irrespective of the owner's nationality. Thus persons domiciled in Italy and enterprises whose statutory seat is in Italy are not liable to tax on land they possess abroad. On the other hand, the tax is due from persons domiciled abroad and enterprises whose statutory seat is abroad, in respect of land they possess in Italy.

¹ Legislation in force on June 1st, 1933.

² The land tax is governed by the basic Law No. 2382, of March 1st, 1886, which has been amended to a certain extent by the Laws of June 20th, 1889 (No. 6130), January 21st, 1897 (No. 23), July 7th, 1901 (No. 321), and July 8th, 1904 (No. 386), and by the Royal Decree No. 2089, of October 23rd, 1909.

Regulations in execution of the basic Law of March 1st, 1886, were approved by Royal Decree on January 26th, 1905, and these were modified by a number of later royal decrees.

EXEMPTIONS.

It would be superfluous to enumerate the various exemptions based either on the nature of the ground or the use to which it is put. It should, however, be noted that the income from land in use as mines, quarries, peat-bogs and salt-works (Law No. 7222, of December 6th, 1923) and income from lakes and ponds used for fishing (Law No. 1260, of July 11th, 1929) is exempt from land tax, but that it is subject to the tax on income from movable wealth and is treated in the same way as industrial or commercial income accruing to the enterprise to which the land belongs.

3. ASSESSMENT OF TAX.

(a) COMPUTATION OF TAXABLE INCOME.

The property yield of land is assessed by the fiscal authorities on the basis of its area and position, geological features and nature of its cultivation, without a return being required of the taxpayer. The owners have certain legal remedies against the assessment by these experts and may appeal to have the income from their land fixed with a closer regard for facts.

Speaking broadly, this form of income (*reddito dominicale*) corresponds to the rental value of the estate.

Once the income is determined, the administration enters it in a special register (*cadastre*) kept as a rule for the territory of every commune in the kingdom and showing the area of the estate, its character, the forms of cultivation and the name of the person having the use thereof (owner, usufructuary or holder on long lease). All transfers of the property *inter vivos* or by inheritance are immediately entered in the register.

The income entered in the register cannot be lowered or raised in consequence of changes in its nature, class or tariff, except by a general revision of the register. Such revision is governed by a special law.

Changes in the classification of land and its income are, however, permitted for certain special reasons indicating either an increase (an alluvial deposit, formation of islands, census of property hitherto not included in a census, revised classification of improved land, etc.) or a decrease (total or partial abolition of property or loss of its productive capacity). It is the duty of the financial administration to take note of these changes and enter them in the register every five years. Further, every taxpayer may claim in respect of any year a revision of the income for which his land is assessed, if the products of that land differ from those mentioned in the register. In this case, the tax is assessed on the revised income as on January 1st of the year following that in which the revision was claimed.

The financial authorities may in their turn proceed in any year to revise the income from land so as to take account of any increase of income resulting from a change in cultivation. In this case, too, the new income is taxed as from January 1st of the year following the year of revision.

In order to avoid inequalities of treatment due to the diversity of cadastral registers, some of which were in existence prior to the unification of the kingdom, while others were established by the Law of 1886 on Land Registers, Law No. 17, of January 7th, 1923, prescribed a general revision of cadastral income with effect as from January 1st, 1925. This revision is based on a revaluation of income in accordance with the prices of agricultural products on January 1st, 1914.

The incomes established by this general revision are therefore expressed in gold values.

(b) COMPUTATION OF TAX.

The rate of tax on these incomes is fixed at 10 per cent, which is very much in the taxpayer's favour, for he has only to pay a tax of 10 paper lire per 100 gold lire of income, expressed, as already said, in gold values. The tax is increased by additional percentages (*centimes additionnels*) which are levied in favour of the provinces and the communes. The normal rate of these "centimes

additionnels" is, as regards those levied on behalf of the communes, 200 centimes per lira of the basic tax, and as regards those collected for the provinces, 50 centimes per lira of the basic tax. In the first case, the "centimes additionnels" may be increased up to 400 and further up to 500, while those belonging to the provinces may only be raised up to 100.

4. COLLECTION OF TAX.

The land tax is paid by the taxpayer himself. It is collected from him in accordance with the general provisions governing the recovery of taxes payable by the taxpayers themselves, which are set forth in connection with the tax on income from movable wealth (pages 254 and 255).

II. TAX ON BUILDINGS.

1 and 2. TAXPAYERS AND TAXABLE INCOME.

The tax on buildings¹ is leviable on the income from buildings, whatever the materials used or purpose of the building.

The tax is payable by the owner of the income — *i.e.*, the person who has the proprietary enjoyment of the building or from one who enjoys a right of usufruct, use, habitation or perpetual lease in respect thereof.

The owner of the income is liable to this tax whatever his nationality or domicile.

EXEMPTIONS.

As already mentioned, the income from mines, quarries, peat-bogs and salt-works, and lakes and ponds used for fishing is not liable to land tax, but makes up part of the total income from industry and is thus liable to the tax on movable wealth. Similarly, the income from buildings used as factories is exempted from payment of the tax on buildings and is included in the assessment of industrial income resulting from the exploitation of the factory (Articles 5 and 6 of Law No. 3069, dated December 30th, 1923).

As regards exemptions properly so called, we would merely mention that all buildings are exempt from tax for the first two years following their erection and that buildings used as dwellings, hotels, offices and business premises, the building of which was begun at a date fixed by the law and which shall have been declared habitable by December 31st, 1935, are exempt from tax for twenty-five years.

3. ASSESSMENT OF TAX.

(a) COMPUTATION OF TAXABLE INCOME AND DEDUCTIONS.

The taxable income is computed either on the basis of the actual income — *i.e.*, the rents as shown in the leases (the financial administration can alter the rent laid down in the contract if it does not think it in accordance with facts), or on the rental value when the premises are not let. In assessing income, account is taken, not only of the building proper, but of any land forming an integral part of it, such as courtyards, gardens, etc.

The net taxable income is obtained after reducing the actual or presumed income by one-third, to represent ordinary and extraordinary costs of upkeep, cost of fire insurance, depreciation, losses resulting from partial failure to let or from total failure to let over a period not exceeding twelve consecutive months. This reduction of one-third is fixed; its application is universal and it cannot be increased or diminished on the grounds that it is no longer in accordance with the facts. Further deductions from the actual or presumed income are costs of minor repairs, tips to *concierges*, water,

¹ The tax on buildings is governed by the basic Law No. 2136, of January 26th, 1865. This law has been constantly amended by further laws, and executive regulations were published in Royal Decree No. 4024, on August 24th, 1877.

light and gas rates, charges for central heating, lifts, etc., when the owner can prove that these expenses fall upon him and not upon the tenant. These expenses, however, are deducted, not in the form of a lump sum, but must correspond to the actual expenditure.

When the net income assessable for tax has thus been determined, it is entered in a special register (*cadastre*) similar to that used for landed estate, but quite distinct from it.

The income shown in the register may be altered in virtue of a general revision resulting from a law. The last real general revision of income from buildings in Italy was undertaken in virtue of Law No. 6214, of July 11th, 1889. The Law of December 30th, 1923, which came into force on January 1st, 1925, provided for a new general revision, but in a purely automatic form, since the administration re-assessed the incomes entered in the register by increasing them by a coefficient larger or smaller according as the assessment on which they were based dated back a long or short time beyond 1923 (this law did not affect incomes assessed between January 1st, 1923, and December 31st, 1924).

For incomes assessed prior to December 31st, 1910, the coefficient was 300 per cent ; prior to December 31st, 1918, 250 per cent ; prior to December 31st, 1920, 150 per cent ; and prior to December 31st, 1922, 50 per cent.

Unlike the measures for re-assessing income from land, to which reference was made above, the general re-assessment of buildings does not express incomes in gold, but in paper lire. We shall see the consequences of this when we come to consider the complementary tax.

Income from buildings may be altered by a partial as well as a general revision.

Partial revisions may serve to correct errors made in the general revision prescribed by the Law of December 30th, 1923.

Their purpose may be to determine the reductions or increases of income at a given time and resulting from permanent causes, provided the increase is not less than one-third and the reduction less than one-quarter of the income determined at that time.

(b) COMPUTATION OF TAX.

The income from buildings is taxed at the rate of 10 per cent. This tax is increased by additional centimes in favour of the communes and provinces. The law fixes this supplementary tax in the form of a certain number of centimes per lira of ordinary tax paid into the Treasury ; the normal proportion is 50 centimes for the communes and the provinces ; it may be raised up to 75 centimes in the case of provinces, and up to 100 centimes or even 125 centimes in favour of the communes.

These additional centimes increase considerably the tax burden on immovable property and they constitute the principal receipt of the provincial and communal budgets.

4. COLLECTION OF TAX.

What has been said above concerning the collection of the land tax applies here also, and the collection of the tax on buildings is governed by the general provisions applicable to the collection of direct taxes, which, as already indicated, is set forth in connection with the tax on movable property (pages 254 and 255).

III. TAX ON INCOME FROM MOVABLE WEALTH.

1 and 2. TAXPAYERS AND TAXABLE INCOME.

In respect of yield, the tax on income from movable wealth (*ricchezza mobile*)¹ is the most important direct tax in the Italian fiscal system.

¹ This tax is governed by the basic Law No. 4021, of August 24th, 1877, to which subsequent laws have added numerous amendments. These we shall refer to in the present report as occasion requires.

For the moment, it need only be said that regulations for executing the Law of August 24th, 1877, were approved by Royal Decree No. 560, dated July 11th, 1907.

The law understands by "income from movable wealth" all income not derived from land and buildings, including income from real property when such property has not been or cannot be assessed for land tax (income such as quit-rent (*cens*), tithes (*dîmes*), income from assignment (*contrats d'antichrèse*) contracts).

The tax on movable wealth is imposed upon income derived in Italy irrespective of its owner; it is therefore levied, not only on income received by individuals, but also on income received by corporations and by commercial companies established *de jure* or existing *de facto*, by non-commercial companies (*sociétés civiles*) formed for some profit-making purpose, by associations, consortiums, etc. The law establishes complete equality of treatment between nationals and foreigners, whether resident in Italy or not.

The tax is leviable upon all products of movable wealth originating in the national territory, whether they are recurrent and periodical or single and non-recurrent, whether they accrue to Italian nationals or to foreigners and whether these two classes of person do or do not reside in Italy. The law regards the following as produced on national territory:

(a) Income entered at Italian offices for the registration of mortgages or resulting from a notarial act and drawn up in Italy;

(b) Salaries, pensions, annuities, interest and dividends paid on behalf of the State, provinces, communes, public institutions and commercial, industrial or insurance companies having their seat in Italy;

(c) Income derived from industries, trades, employments and professions carried on in Italy and, generally, every kind of income, other than from land and houses, when such income is *produced* in the kingdom or payable by persons domiciled or resident in the kingdom.

This last paragraph necessitates some explanation as to (1) what the law means by "domicile" and by "residence", and (2) the cases in which the law considers that an industrial, commercial or professional income originates in the country.

1. The fiscal laws do not contain any special clause defining the domicile or residence of taxpayers; in this matter, the provisions applicable, even for fiscal purposes, are those of the Italian Civil Code, Article 16 of which defines domicile as the place where a person has the principal seat of his business and interests. This definition applies both to individuals and companies. Thus, as regards the latter, the domicile is the place in which they have their seat, which place must be specified in the articles of association and in the company's statutes (Articles 88 *et seq.* of the Commercial Code). A company whose articles of association were drawn up in Italy, but which establishes its seat in a foreign country, is not regarded as domiciled in Italy. On the other hand, a company constituted abroad which fixes its seat in Italy is regarded as domiciled in the country.

As regards residence, Article 16 of the Italian Civil Code lays down that a person's residence is in the place where he customarily resides — that is, the place where it is his habit to live — although it may not be the seat of his business and interests. This conception of residence can obviously apply only to individuals and not to companies.

2. The existence or production of income within the national territory means that the taxpayer is liable to tax on all income he receives in Italy and also on income he receives abroad, if the centre of his productive activity is in Italy.

An exception to this rule is allowed when the enterprise, while having its centre of management (central seat) in Italy, has established branches abroad. In such cases, the law exempts from tax on movable wealth the income resulting from the activities of the foreign branch. This exemption, however, is conditional upon the branch's keeping entirely separate accounts from those of the central seat and upon the enterprise submitting all the evidence necessary to determine the nature of the income to be ascribed to the subsidiary or branch and of the income to be ascribed to the central seat (Article 9 of Law No. 1463, dated August 12th, 1927).

All the above provisions apply also to branches established in the Italian colonies, provided these colonies have a fiscal organisation independent of that of the mother country.

Subsidiaries created abroad in a legally independent form are never liable to tax on movable wealth in Italy in respect of their foreign activities, even when they are controlled by, or are the full property of, the Italian company.

Nevertheless, the income received by the parent company in Italy is reckoned for the purpose of assessing the net taxable income of the said parent when it is the result of exercising the said control or right of ownership and when it appears, after deducting expenses, among the assets in the balance-sheet of the Italian company.

In practice, however, as the outcome of administrative interpretations and methods of application, the Treasury allows Italian companies in certain specific cases not to include among assets, for purposes of assessment, income which they can prove to be derived from the exercise of control over subsidiaries, or from the property of subsidiaries abroad, when this situation results from the possession of foreign shares of the said subsidiaries.

As applied to foreigners, the taxation of income derived in the national territory means that the Treasury assesses these foreigners in respect of all income they receive in Italy, even if the centre of their activities is abroad, but provided *they have a permanent productive organisation in Italy*. This organisation may be a branch, a representative's office, an agency, a purchase and sales office, an establishment, a warehouse, goods depôt, etc.

Accordingly, if a foreigner in Italy engages in purely occasional and isolated operations, or even in continuous transactions through a mere commercial traveller or an intermediary having the character of a really independent agent, and if, further, he has in Italy no permanent productive organisation involving any kind of continuous and direct activities in Italy, that foreigner is not liable to tax on movable wealth in respect of the income from these transactions, unless the latter are recorded in one of the deeds mentioned above under (a).

EXEMPTIONS.

The law provides for various exemptions from the tax on movable wealth, exemptions both permanent and temporary. Amongst the numerous permanent exemptions from the tax, we may mention the following :

(a) Income which, according to the law, is already assessable for tax on movable wealth.

On this ground, a shareholder in a joint-stock company cannot be taxed on dividends distributed by the company, because these dividends have already paid the tax in the form of profits of the distributing company.

Similarly, a person who deposits savings in a bank cannot be taxed on the interest on that deposit, because, subject to the right to recover, the bank itself is taxed on that interest.

(b) Interest on public debt and Treasury bonds.

(c) The premium on issues of new shares — that is, the difference between the value of a company's old shares and the price of the new shares issued by the company, whether they are offered to the public or whether given to the old shareholders on option.

(d) Interest on loans contracted by corporations, companies, or individuals for the construction and purchase of workmen's dwellings.

(e) Interest on loans granted by certain credit institutions (*institutions de crédit foncier*) lending on the security of real estate.

(f) In the case of agricultural credit operations facilitated by certain special organs and institutions authorised for this particular purpose, the fiscal law establishes a flat rate of taxation (*abonnement*) of 10 centimes per 100 lire of capital used. This method of taxation includes the duties on agricultural credit transactions and the tax on movable wealth, whether levied on the income from the said credit operations or on the interest from bonds and on productive assets.

(g) A very important exemption is that enjoyed by the *interest on bonds issued by the provinces, municipalities, corporations and share companies*. The purpose of this exemption is to encourage investment in works of public utility and national industries (Article 10 of Law No. 1643, dated September 20th, 1926).

This exemption is only granted to bonds issued since the entry into force of the Law on September 30th, 1926. The exemption extends to bonds issued in Italy as well as to bonds issued abroad.

The law has special clauses dealing with loans contracted and bonds issued abroad by national companies of all kinds, by companies constituted abroad but having their seat and principal object of their enterprise in Italy, by municipalities and provinces or, finally, by other regularly constituted organs such as the consortiums.

Law No. 1634, of December 16th, 1922, authorised the Government to exempt from the tax on movable wealth interest on loans contracted abroad and bonds placed abroad by the above-mentioned organs, on condition that these bonds were not then brought into circulation in Italy. The Law No. 1635, of September 4th, 1925, has also empowered the Government to grant exemptions in connection with duties and fees on transactions.

Law No. 2162, of December 10th, 1923, and Law No. 1, of January 5th, 1928, concerning loans contracted in any form abroad, prescribe previous authorisation by the State.

Law No. 130, of March 13th, 1930, provides that the above-mentioned fiscal exemptions may be granted to loans and bonds contracted or placed abroad before December 31st, 1933.

It appears from the foregoing explanations that, under Law No. 1643, of September 20th, 1926, all bonds issued in Italy or abroad since September 30th, 1926, are exempt from the tax on movable wealth. As regards bonds issued abroad prior to September 30th, 1926, these only enjoy fiscal exemption when this is granted by the State.

(h) Lastly, Law No. 857, of May 7th, 1925, allows the Government to exempt from the tax on movable wealth foreign shipping enterprises with branches, agencies or representatives in Italy, in respect of income derived from the exercise of maritime transport in Italian ports, provided that the same facilities are granted reciprocally to Italian shipping enterprises by the foreign States whose shipping companies are exempted in Italy.

This exemption is enjoyed by American shipping companies with services in Italy (Royal Decree No. 891, of June 11th, 1925) and by Italian shipping companies with services in the United States.

In addition to these permanent exemptions, Italian law provides for numerous *temporary exemptions* granted for a number of years to works scientifically organised and erected in certain parts of the country or in certain towns (Naples) or in an industrial zone within the jurisdiction of certain ports (Venice, Leghorn, Fiume, Pola, etc.) ; also to scientifically organised industries in any part of the country for the extraction of essences from flowers and the manufacture of scent ; to works for drawing off water built on certain rivers and basins and to electric power-stations ; lastly, to establishments that consume the energy thus produced.

Other temporary exemptions affect special industries like fishing and pisciculture, the building of merchant ships for Italian nationals, etc.

3. ASSESSMENT OF TAX.

(a) COMPUTATION OF TAXABLE INCOME AND DEDUCTIONS.

The taxation of income from movable wealth is based upon a classification of the income itself in different categories according to the elements which combine to produce it (Law No. 1613, of October 16th, 1924).

These categories of income from movable wealth are five in number, each designated by a letter of the alphabet.

Category A includes income derived exclusively from capital, such as interest on loans.

Category B includes income produced by co-operation between labour and capital, such as industrial and commercial income.¹

Category C1 includes income of an uncertain and variable nature derived from labour and the exercise of a profession.

Category C2 includes income from labour in the form of certain and definite amounts, as in the cases of salaries, allowances, pensions, etc. It also includes income, such as annuities, which is produced without any effective contribution by capital or human labour.

Category D includes income from labour in the form of certain and definite sums, such as salaries, pensions and allowances paid by the State, provinces, municipalities, public welfare institutions, learned associations, provincial economic councils (former Chambers of Commerce) travelling schools of agriculture.

The rules for the determination of the taxable amount which are common, if not to all the categories of income mentioned above, at least to several of them, will first of all be set forth, and then an examination will be made of the rules special to each of them.

Returns and Bases of Assessment.

Except income belonging to Categories A and D, which is withheld at the source, all income is assessed on the basis of a return made by the taxpayer or by his legal representative.

The return must mention the different items of each category and, for each item, state the gross income, expenditure, annual charges on liabilities and net income.

Individuals.

Individuals liable to income tax must submit their returns to the revenue office within whose jurisdiction the taxpayer is domiciled before January 31st of the year following that in which the income was first produced. The only exception to this is Category C1 income, which must be declared not later than January 31st of the second year following that in which it was first produced.

The revenue authorities are entitled to correct the declaration if they think it does not correspond to facts. If the taxpayer has failed to make a declaration, the authorities assess on their own

¹ With regard to profits from agriculture, only those derived by farmers come within the scope of the present category. The income which an owner who cultivates directly his own land or lets it to a tenant other than a farmer (*métayer, colon partiaire, i.e.*, a tenant who does not pay a fixed rent in cash, but a rent which varies according to the yield of the property and which is usually in kind or partly in cash and partly in kind) as well as the income from such tenants are subject to the "tax on agricultural income" regarded as income from movable wealth (see pages 255 and 256).

initiative. This assessment, however, can only cover the current year and the two previous years, for, as regards earlier years, action by the Financial Administration is barred by limitation.

The revenue office must inform the taxpayer of corrections made in his declaration or of an assessment made in the absence of a declaration.

Income of a fixed and definite amount (Categories A, C2 and D) is assessed on the basis of the exact amount of this income. This is the reason why the taxpayer is required to declare any increase of income and has the right to claim a reduction of tax on the grounds that his income has diminished. On the other hand, as regards income of an uncertain and variable nature (Categories B and C1) received by private taxpayers, the assessment, once made, cannot be reduced at the taxpayer's request until two years after it was made. Nor can it be increased at the suggestion of the revenue authorities unless four years have passed. If, however, at the end of two years, the taxpayer asks for a reduction, the authorities may reply with an increased demand, being, in these circumstances, under no further obligation to observe the four years' limit.

In the case of either a reduction or an increase, the administration, in correcting the assessment of income subject to change or variation, will consider the average income for the two previous years.

Companies.

Share companies, credit institutions and savings banks must submit to the revenue authorities every year a declaration of their income within three months of the date when the balance-sheet was approved and, in any event, not later than December 31st.

As a rule, the authorities are required to have the different balance-sheets suitably checked before assessing on their results.

If, however, there are good reasons for thinking that the balance-sheets are not correct, the revenue authorities may disregard the results shown therein and may assess on a presumed income — that is, by fixing an income figure in the light of all available evidence.

The law lays down special rules for the taxation of all share companies (corporations and limited partnerships) and of credit institutions and savings banks.

In the case of Category B income, share companies, credit institutions and savings banks are not subject to the rule which lays down that the assessment cannot be changed for the space of two or four years. The Treasury taxes them on the basis of their balance-sheets, as follows :

Once the company is constituted, the data furnished by the first balance-sheet serve as the basis of the tax for the first and third years of operation ; the data furnished by the second balance-sheet serves as the basis of the tax for the second and fourth years of operation, and thereafter the third balance-sheet's data serve for taxing the fifth year's operations, those of the fourth balance-sheet for taxing the sixth year, and so on, in accordance with the method known as " alternate balance-sheets " (*rotation des bilans*). It should be added that the jurisprudence of the day does not regard the use of this method as a case of deferred taxation. It was only desired that taxation in any given year, instead of being based upon the balance-sheet results for that year, should be based upon the results of the balance-sheet of the second year before the year for which tax was being collected ; this tax, however, is the tax due for the year for which it is collected and not the tax due in respect of the year of the balance-sheet taken as the basis of assessment.

Should it happen, therefore, that the actual balance-sheet (*i.e.*, the balance-sheet of the year for which the tax is being collected) shows an income higher or lower than that resulting from the alternate balance-sheet method, the financial administration is not allowed to make a further assessment in order to reckon the difference between the two incomes, nor is the company entitled to claim refund of the tax paid by it on the difference.

Exception to this rule is made when the actual balance-sheet shows no taxable income, but a deficit ; in this case, the company may claim refund of the tax paid on the basis on which the assessment made on the alternate balance-sheet system, provided it makes a formal claim to this effect within the period prescribed by the law (Article 7 of Law No. 1643, of September 20th, 1926).

Partnerships.

Partnerships are taxable as corporations, but their assessment is in accordance with the procedure and methods applicable to individual taxpayers. The partners are liable for the payment of the tax for which the partnership is assessed, not only on the property used for the partnership's business, but also on their private property, in accordance with the principle of unlimited liability.

Deductions.

Income from Category A. — This income is taxed on its whole amount without any deduction whatever.

Income from Category B. — Income belonging to Category B is liable to the tax on movable wealth after deducting :

- (a) Charges on liabilities ;
- (b) Costs of production.

The tax is therefore on *net*, not *gross*, income.

(a) *Charges on Liabilities.* — The Treasury understands by these charges any interest that the taxpayer has to pay on debts incurred by him in the establishment, management, maintenance or improvement of the enterprise from which he obtains the income assessable for tax on movable wealth.

Consequently, before charges on liabilities can be deducted from gross income, the following condition must be fulfilled : the payment of these charges must be directly connected with the production of income, in such manner that the charges have to be paid before the income can be earned.

An industrial enterprise, for instance, may deduct interest on debts it has incurred in buying its machinery.

For purposes, however, of deducting charges on liabilities, a distinction must be made between enterprises constituted as (1) share companies and (2) other enterprises.

(1) In the case of the former, these charges are deducted from the gross income of Category B and the enterprises are then taxed on them as income belonging to Category A. These enterprises, of course, are entitled to recover the tax paid from their creditor.

As regards commercial companies and insurance companies (mutual and non-mutual), the fiscal authorities do not allow any deduction from the taxable income of sums employed for increasing the company's capital, for the payment of its debts, or for transfers to its reserve fund (except for the mathematical reserves of insurance companies). The tax on movable wealth is in fact an impersonal tax — *i.e.*, a tax which is levied on income merely because such income exists and is due at the time such income is realised, no account being taken of the person receiving it or of the use for which it is destined.

(2) In the case of individuals or enterprises other than share companies, charges on liabilities are deducted from the gross income of Category B, provided that the debtor furnishes the name and domicile (in Italy) of the creditor, so that the interest may be assessed as Category A income, for which tax may be claimed from the person who receives it.

If the name and domicile of the creditor have not been stated or if the creditor is domiciled abroad, the administration does not allow deduction of interest, but includes it among the taxable income of Category B and claims tax from the debtor, who can recover from his creditor.

On the other hand, the creditor may be a trader or manufacturer who has lent his money, not as an ordinary investment of capital, but for reasons connected with his industry or trade. In that case, the Treasury allows the debtor to deduct interest paid out of his income in Category B

without claiming tax on it from the same debtor as income belonging to Category A. In this case, in fact, the Treasury has to claim the tax directly from the creditor as income belonging to Category B.

The same applies to interest paid by banking enterprises to their depositors. If the deposits are savings bank deposits, which are a simple investment of capital, and if, further, the banking enterprise is a share company, the Treasury deducts interest on income in Category B payable by the credit banking enterprise but taxes the latter on it as Category A income, the enterprise having the right to recover from its creditor. If the banking enterprise is not a share company, the Treasury allows deduction of interest on condition that the establishment furnishes the name and (Italian) domicile of the creditor. Otherwise, the deduction is not allowed.

In the case of current account deposits of a commercial character, the Treasury deducts interest on income received by the banking enterprise under Category B, but without taxing it as income belonging to Category A. In this case, the Treasury includes this interest as the creditor's income in Category B.

(b) *Costs of Production.* — These consist of all the expenses necessary to produce the income — viz., cost of using raw materials, instruments, machinery, material, etc., salaries of employees, workmen's wages, rent of premises, etc.

The only costs therefore that can be deducted from income in Category B are those without which no income could be produced. On the other hand, no costs may be deducted which represent an allocation or re-employment of income already produced, such, for example, as the payment of direct taxes on the enterprise's income itself.

The costs of production include allowances for the depreciation of industrial plant. They also include the amortisation allowances of industrial installations, but — for fiscal purposes — only if the latter are intended for public services (tramways, railways, etc.) and when those services are the object of a concession granted in return for an undertaking on the part of the concessionary to surrender all the installations to the conceding authority without claim to compensation, on the expiration of the concession. In practice, this strict rule is somewhat relaxed in that certain allowances for depreciation calculated at an annual lump sum finally include the amortisation allowances and become identical with these, if not in the accounts, at any rate in fact.

Income from Category C1. — Income in this category is subject to the same rules as Category B income as regards the deductions representing charges on liabilities and costs of production.

In the case of these charges and costs, it is not, of course, possible to apply to income belonging to Category C1 (professional income) all the rules which apply especially to income in Category B — *i.e.*, industrial and commercial income.

Artisans' income is taxed as Category C1 or Category B, according as the most important factor in the working of the enterprise is manual labour pure and simple or the employment of capital.

Income from Category C2. — On income in Category C2 the Treasury allows no reduction for costs of production. It does, however, grant reductions for charges on liabilities. The latter may, for instance, be deductions from salaries paid into a provident or pension fund for the benefit of those who receive these salaries.

Income from Category D. — The rules governing the determination of the taxable amount for the income in Category C2 apply also to income in Category D.

Methods of checking Returns.

In order to facilitate the verification of returns, the law (Article 37 of Law No. 4021, of August 24th, 1877) has entrusted the revenue authorities with certain powers by which they may :

- (1) Call upon the public officials to forward any documents that may be needed ;

- (2) Summon the taxpayer to appear in person or through a legal proxy to furnish explanations or evidence ;
- (3) Instruct one of their own officials to inspect industrial or commercial premises ;
- (4) Summon any persons who are able to supply information concerning the activities of the various taxpayers ;
- (5) Inspect the registers of share companies (Article II of Royal Decree No. 360, dated January 28th, 1929, entitles the revenue authorities to inspect also the registers which other companies than share companies and individuals are required to keep in accordance with the Commercial Code) ;
- (6) Demand to see the scrip or certificate of fixed income (Category A) ;
- (7) Take account of the rental value of a taxpayer's house as an index by which to determine the industrial and commercial income of professional men.

Apart, however, from all the methods of recourse specially mentioned in the law, the revenue authorities may also have recourse to other sources of information in order to verify taxpayers' returns or determine the taxable income by their own initiative when the taxpayer has failed to make a return. The authorities may take what measures they think fit to obtain all particulars that may help them to fix the exact taxable income. They may further enlist the aid of the public safety department, the royal *gendarmerie*, the heads of the administrative services of the State, provinces and municipalities, public bodies and, finally, of the "fiscal enquiry police" (*polizia tributaria investigativa*), a force consisting of military policemen belonging to the Royal Revenue Guard, whose particular duty is to punish fiscal offences of all kinds.

Appeals.

The taxpayer may appeal against measures taken by the revenue authorities, whether these relate to assessment in the absence of the taxpayer's declaration, to a correction of that declaration or to a revised assessment increasing the income as previously assessed, after expiration of the four years during which the figure cannot be altered.

An appeal must be lodged, on pain of foreclosure, within twenty days of the notification of assessment.

If, on the other hand, appeal is lodged in due time, the dispute between the taxpayer and the revenue authorities may be adjusted by a friendly agreement known as a *concordat*. If no compromise is reached, the dispute is submitted to the judgment of special judicial bodies known as *Administrative Committees for Direct Taxes*.

The special jurisdiction in the matter of direct taxes involves three instances :

- (a) The first instance is the *Commissione Mandamentale*, so called because there is one for each *mandamento* (corresponding to the French *arrondissement*) ;
- (b) The parties may appeal against the findings of these committees of first instance to a committee of appeal existing in each province, such committees being known as *Provincial Committees for Direct Taxes* ;
- (c) Appeals against the decisions of the provincial committees may be lodged with a *Central Committee for Direct Taxes*, the seat of which is in Rome at the Ministry of Finance and the jurisdiction of which extends to the whole of Italy.

In principle, this Committee is not competent to judge questions of pure fact or assessments of income, for appeal may only be made to it on questions of law, as it is, mainly, the supreme court of appeal in fiscal matters.

The findings of the committees have to be notified to taxpayers by the revenue office which first assessed the tax. This notification is made in accordance with the same rules and formalities as those which are applicable in connection with the notification of quotas and corrections.

Appeal must be made to the Provincial Committees against the findings of the *Mandamento* Committee, and to the Central Committee against the decisions of the Provincial Committees, within twenty days of receiving notification of the judgment appealed against. Once this term has expired and the office has not told the taxpayer that it intends to appeal against the judgment and if, at the same time, the taxpayer has not lodged his own appeal and obtained a receipt for it, the judgment of the *Mandamento* or Provincial Committee becomes final and is no longer open to dispute.

If, however, the tax is entered on the collection lists (*rôles de recouvrement*), the taxpayer may protest against its entry if he wishes to prove that the quota or judgment was not duly notified to him, or if the revenue office has committed a material error in drawing up the lists, or if the income assessed does not in fact exist, or, finally, if the same income has been taxed twice. If the office admits the validity of the taxpayer's plea, it takes the necessary measures. If it does not, it dismisses the appeal, but the taxpayer may still carry his case before the committees.

Judgment by the committees does not altogether exhaust judicial procedure in the matter of direct taxes, for the law allows the ordinary courts to receive appeals against the findings of these committees. The courts, however, are not competent to judge questions relating solely to the assessment of taxable income.

Appeal to the judicial authorities must be accompanied by proof that the whole amount of tax due has been paid, subject to its refund if judgment is given in favour of the taxpayer.

The right of recourse to the judicial authorities lapses after six months from the date of the publication of the lists on which the tax was entered or from the day on which the tax was deducted.

(b) COMPUTATION OF TAX AND ABATEMENTS.

Income from Category A. — Income of this category is liable to tax whatever may be its amount and on the entirety of such amount at the rate of 20 per cent.

Income from Categories B, C1, C2. — The rates of tax are : 14 per cent for Category B incomes except for profits derived by farmers¹ from agriculture ; in this case the tax amounts to 7 per cent ; 12 per cent for Category C1 ; and 9 per cent for those from Category C2.

There are certain provisions regarding taxation common to these three categories of income. Firstly, they are only taxable if they amount to 2,000 lire a year or more.

Further, small incomes between 2,000 and 2,500 lire are not taxed in their entirety, the Treasury, before imposing the tax, deducting a fraction calculated as follows :

On incomes up to 2,100 lire, the deduction is 1,000 lire ; on incomes between 2,101 and 2,200 lire, 800 ; between 2,201 and 2,300 lire, 600 ; between 2,301 and 2,400 lire, 400 ; and between 2,401 and 2,500 lire, 200.

In order, however, to determine the taxable minimum of 2,000 lire, account is taken, not only of movable wealth of all categories, but also of income from land and houses. Thus income from movable wealth amounting to 1,000 lire is liable to the tax if the taxpayer has another 1,000 lire of income from immovable property. In connection with the exemption which certain salaries coming under category C2 enjoy in practice, see page 255.

Income from Category D. — Income from this category is taxed in principle at 8 per cent. The rules set forth on the subject in connection with the income from Categories B, C1 and C2 as regards exemptions and deductions apply only if the income of these categories is paid by bodies other than the State.

On the contrary, salaries and wages paid by the latter are taxable on their entire amount.

¹ See note on page 248.

Further, it should be noted that, in connection with wages of workmen employed by the State, provinces, municipalities and the various autonomous enterprises organised by the State, the provinces and the municipalities, by railway enterprises, urban and inter-urban tramway enterprises, inland navigation lines, by public motor services and telephone companies, the rate applicable is 4 per cent.

4. COLLECTION OF TAX.

(a) BY DIRECT PAYMENT.

As a general rule, only taxes due on income from Categories B and C₁ are payable by the taxpayer himself. At the same time, although income from Category A is, in general, taxed in the same way as income from Categories C₂ and D — *i.e.*, by withholding at the source — in the case of interest paid by individuals or by public bodies other than provinces, municipalities, legal entities or share companies, it is the creditor himself who pays the tax direct.

The collection of these taxes is subject to the general rules for the collection of taxes which have to be paid by the taxpayer himself.¹ It is governed by Law No. 1901, of October 17th, 1922, and by Royal Decree No. 2090, of September 15th, 1923, which have been subsequently amended.

The provisions governing collection are the following :

The annual taxes due from every taxpayer are entered on the collection lists (*rôles de recouvrement*) and these lists are given executory force by the Superintendent of Taxes (*Intendente di Finanza*) in each province. They are first published in each commune for a week, in order that every taxpayer may take note of them and, if there is occasion, appeal against them. They are then forwarded to the collector of taxes and constitute the warrant in virtue of which he can proceed to collect, if necessary by coercive means.

Collection lists are of two kinds :

- (a) Main lists ;
- (b) Supplementary lists.

The main lists relate to taxes due for the year for which actual collection is being made. They must be published in each commune for a week, the last day of which must not be later than January 10th in each year.

The supplementary lists relate to taxes due in respect of years preceding the year of collection. They are divided into *supplementary lists (first series)*, which, like the main lists, must be published for eight consecutive days before January 10th, and *supplementary lists (second series)*, which have to be published for eight consecutive days before July 10th in every year.

The taxpayer is required to pay the taxes on the main lists and on the supplementary lists (first series) in six two-monthly instalments, the first of which corresponds to the months of January and February. Taxes on the supplementary lists (second series) are likewise payable in two-monthly instalments, the first corresponding to the months of July and August and the last to the months of May and June of the following year.

Once in possession of the lists, the collector has to deliver to each taxpayer a note stating the amount of each two-monthly payment.

The different two-monthly payments fall due on the tenth day of the second month in each group of two months. If the taxpayer has not paid within twelve days of payment falling due, the collector adds interest at 2 per cent, which rate is increased to 6 per cent if payment is delayed beyond another twelve days.

¹ As stated elsewhere, the rules set forth below are also applicable to the recovery of taxes on buildings, on land and on agricultural income regarded as personal property, and of additional tax.

In addition to fines, the law enacts special penalties for taxpayers who are in arrears with the payment of six or more successive instalments of direct tax.

(b) BY WITHHOLDING AT THE SOURCE.

In principle, as is set forth in detail below, incomes from Categories A, C₂ and D are only paid to their beneficiaries by the debtors after deduction of the amount of the tax.

Income from Category A. — When interest is paid by the State, it collects the tax at the source, deducting the amount of the tax from the sum paid.

When provinces, municipalities, corporations and share companies pay interest on debts they have contracted, the tax on movable wealth is payable by the debtor, who may recover it from his creditor in the form of a deduction at the time of paying interest.¹

If, on the other hand, interest is paid by individuals or by associations other than provinces, municipalities, corporations or share companies, the tax is payable directly by the creditor who receives the interest.

Income from Category C₂. — The essential characteristic of the taxation of this category of income is that normally the tax is not collected directly from the recipient of the income, but from the employer of labour, whether a company, corporation or individual, who pays the salary, pension or allowance, with the right to recover it from the actual beneficiary. Accordingly, the Treasury allows these payments to be deducted from the gross income in Category B or C₁ accruing to the employer of labour, who is then liable to tax on Category C₂ income, subject to the right of recovery.

Although wages paid to workmen come under Category C₂ and are subject to the same fiscal rules as salaries, in practice, the administration does not tax the wages of workmen who are engaged in purely manual labour and are easily replaced. It confines taxation to the wages of workmen engaged on work of a special character or requiring special skill, and whose employment may therefore in practice be considered to some extent as permanent.

Income from Category D. — The tax on income from movable wealth consisting of salaries, allowances, compensation and wages paid by the State is collected by directly withholding the amount of tax from the sum due.

When salaries, allowances, pensions, etc., are paid by institutions other than the State and when the law taxes these salaries, etc., as Category D income, the tax is collected on the basis of the pay-rolls. The institutions required to pay the wages, allowances, etc., are liable to this tax, reserving to themselves the right of recovery.

The tax on wages of workmen liable at the rate of 4 per cent is not collected at the source or on the basis of pay-rolls; it is withheld by the institution making the payment and paid by it to the office responsible for collecting the tax or to the national exchequer.

IV. TAX ON AGRICULTURAL INCOME REGARDED AS MOVABLE WEALTH.

Tax on agricultural income regarded as movable wealth² is payable on agricultural income derived from land situated in Italy, whatever be the nationality, domicile or residence of the beneficiary of such income.

Agricultural income is considered industrial income, because it belongs to that part of the income from land which is not "estate" income (*revenu domanial*) and is the result of the developing capital put into the land and of the human labour employed to cultivate it.

¹ Any contract placing the onus of paying the tax on movable wealth upon the creditor is null and void in the eyes of the financial administration, which in every case reserves the right to recover the tax from the debtor.

² The taxation of agricultural income as movable wealth instituted by Law No. 16, of January 11th, 1923, for which executive regulations were issued in Royal Decree No. 505, of May 12th, 1923.

Cultivation, it may be remembered, is not confined to harvesting the products of the soil or utilising the live-stock maintained on that land (*revenu domanial*), but extends to the successive operations designed to secure the best conditions for selling the products thus obtained. Agricultural income may be said to be earned to the extent that the products of the soil are first treated for the purpose of making them useful and preserving them. Every operation, on the other hand, which goes beyond utilising and preserving products, is a source of income liable to the general tax on movable wealth.

Agricultural income is classified as Category B income, but the method of its taxation differs in two respects from the taxation of all other income in that category ; the rate of the tax is different and so is the assessment of the taxable minimum.

Whereas the rate of tax on income from movable wealth in Category B is fixed at 14 per cent, agricultural income is taxable at 5 per cent if it belongs to the owner who cultivates his own land either directly or through a steward. If, however, the land is cultivated by a tenant other than a farmer (*colon* or *métayer*), the fraction of agricultural income accruing to the owner continues to be taxed at the rate of 5 per cent, but the tenant's fraction is liable at 2½ per cent.

This regime does not apply to the agricultural income realised by a farmer, which is taxed, as said in note 1 on page 248, according to the rules normally applicable to income of Category B. But the rate of tax is, in that case, 7 per cent instead of 14 per cent, as said on page 253.

Further, the taxable minimum for agricultural income is not 2,000 lire but 534 lire.

When land tax is refunded owing to earthquakes or atmospheric disasters, the revenue authorities also have to refund the tax on agricultural income, both to owners and to tenants.

For the rest, the tax on agricultural income is subject to the same rules that govern the application of the general tax on movable wealth, including the provisions relating to assessment procedure and to appeals.

V. COMPLEMENTARY TAX.

1 and 2. TAXPAYERS AND TAXABLE INCOME.

Unlike all the other direct taxes, which are impersonal taxes, the complementary tax¹ is a personal tax leviable upon individuals only and therefore not on legal entities or companies, whether these are share companies, partnerships or simple *de facto* associations.

It is imposed on the total income of taxpayers, whatever its nature or origin. The factors, therefore, which make up total income are the income from land and houses and all income from movable wealth in the possession of each taxpayer.

It is not the production of income but the enjoyment of it which renders the recipient liable to this tax. Thus the principle of the "territoriality" of the tax, which, as we have seen, is the principle governing impersonal taxes, does not apply here unrestrictedly. Complementary tax is applied with reference to a person's contributive capacity and is therefore based, not only on the "territoriality" of the income, but on its enjoyment and consumption.

For this reason, the taxpayer is assessed for complementary tax, not in the place of his domicile, but in the place of his residence or, in the absence of a residence proper, in the place where he is living.

The following provisions apply to complementary tax in its relation to the nationality of taxpayers :

(a) Income derived and consumed in Italy by an Italian national or a foreigner resident in Italy is liable to tax in its entirety ; a foreigner is deemed to be resident in Italy if he has been living in the country for at least a year ;

¹ This tax was instituted by Law No. 3062, of December 30th, 1923. The rates applicable to this tax were published in Royal Decree No. 177, of February 19th, 1925.

- (b) Income derived in Italy by an Italian national resident abroad is liable to the tax ;
- (c) Income derived abroad by an Italian national resident in Italy is exempt only in respect of the fraction consumed abroad ;
- (d) Income derived in Italy by a foreigner resident abroad is liable ;
- (e) Income derived abroad by a foreigner resident in Italy is liable ;
- (f) Should the Italian national and the foreigner reside part of the year in Italy and part abroad, tax is levied on the fraction of income derived and consumed in Italy.

3. ASSESSMENT OF TAX.

(a) COMPUTATION OF TAXABLE INCOME AND DEDUCTIONS.

The rules regarding returns, methods of checking returns and appeals which apply to the tax on movable wealth (pages 251 and 252) are also in principle applicable here.

The total income liable to complementary tax is obtained by adding together the income already liable to land tax, buildings tax and tax on movable wealth, with the sole difference that the figure taken as the income from land is not the figure assessed for land tax or the figure entered in the land register, but that figure multiplied by three. The reason for this is that the income from land is expressed in the register in gold lire and has therefore to be converted into paper lire.

A married woman's income is included with that of her husband. If she is judicially separated and living apart from her husband, she is separately assessed in respect of any income at her own disposal.

It should be mentioned that, in assessing total income for purposes of complementary tax, the Treasury takes into account, not only income already liable to the impersonal taxes, but income on which the taxpayer pays no impersonal taxes, for the reason that it is exempt in virtue of the general laws of taxation or some special law. Thus, to take an example, even the interest on public debt or Treasury bonds contributes towards the total income liable to the complementary tax.

On the other hand, since this tax has to be adapted to the actual contributive capacity of each taxpayer, the total income established as above is subject to deduction of all expenses and liabilities by which its enjoyment is limited.

These are as follows :

(a) Expenses and losses incurred by the taxpayer in producing the income of all kinds that makes up the total income, except, of course, those expenses and costs already deducted for purposes of the impersonal taxes ;

(b) The taxes and charges of every kind paid to the State, provinces and communes, contributions to public utility concerns, the provincial economic council, trade unions and, generally, all taxes and charges due to organs authorised to levy contributions, except, of course, complementary tax itself and the supplementary charges connected with it ; the deduction of taxes and charges is conditional upon their being in relation to the income serving to make up the total income liable to additional tax each year ;

(c) All interest *whatever* on liabilities which is paid by the taxpayer, provided that this interest is liable to complementary tax in the hands of the person to whom it is paid ;

(d) Contributions paid by law or under a contract into provident funds against sickness, disablement and old age ;

(e) Life insurance premiums.

After deduction of all the above taxes, charges, expenses and liabilities, the total income remaining constitutes the net income assessable for complementary tax.

The assessment of complementary tax holds good for three years, during which time it may not be increased by the revenue authorities or reduced in favour of the taxpayer.

It may happen, however, that during these three years the total income is diminished by more than 50 per cent either (a) because labour has ceased to produce an income or (b) because some of the factors of production appearing in the income assessed are lost or have become wholly unproductive. In both these cases, and in these cases only, the law allows a proportionate refund of tax.

(b) COMPUTATION OF TAX AND ABATEMENTS.

The function of complementary tax in the Italian fiscal regime is to co-ordinate the direct-tax system constituted by the three impersonal taxes and to remedy inequalities of treatment due — in the application of these impersonal taxes — to the proportional character of the tax rates:

This result the law aims at attaining as follows :

(1) By exempting from complementary tax all taxpayers whose total net income is less than 6,000 lire and, after deduction of the allowances for dependents (see below), does not reach 3,000 lire ;

(2) By allowing an abatement of one-twentieth of the income for each member of the family dependent upon the taxpayer, excluding the latter and his wife. These abatements, however, may not exceed 3,000 lire for each member of the family dependent upon the taxpayer.

(3) By fixing a sliding scale starting at 1 per cent for the minimum income of 3,000 lire and rising to 10 per cent for incomes of one million lire and over, the scale being graduated more steeply as the income rises.

Income from personal property belonging to Category D counts as part of the total income liable to complementary tax, but a special fixed rate of one-half per cent is applied to it. All other income is subject to the general rate corresponding to the total income figure, including Category D income.

4. COLLECTION OF TAX.

Complementary tax is, in principle, always paid by the taxpayer himself, and the manner of recovery is that set forth on pages 254 and 255 in connection with the tax on income from movable wealth.

But the complementary tax due on salaries and pensions paid by the State (Category D income) is withheld at the source.

When salaries and pensions are paid by other bodies than the State, though placed in Category D, the administration assesses and collects the complementary tax (at the fixed rate of one-half per cent) from the source of payment, subject to the latter's right to obtain refund.

Although, as regards salaries and pensions paid by ordinary employers, the rule set forth above applies and there is no need to withhold complementary tax (which is paid by the taxpayer), it must be noted that employers are required to furnish the revenue authorities with the names, Christian names and status of their subordinates, together with the salaries paid them, in order that the authorities may check the accuracy of the returns which the employee is still required to make on his own account.

VI. BACHELOR TAX.

The bachelor tax was introduced by Law No. 2132, of December 19th, 1926, to which executive regulations were added in Royal Decree No. 124, of February 13th, 1927.

Foreigners, even those residing or domiciled in Italy, are never liable to this tax. For the purposes of this study, therefore, the existence of this tax need only be put on record with the observation that, in principle, it consists of a fixed tax varying according to the age of the taxpayer and of an increase by half of the complementary tax to which he is liable.

PART II. — TAXATION OF FOREIGN AND NATIONAL ENTERPRISES

Italian law contains no definite provisions governing the questions raised in this part of the present study, and the following account is based upon such jurisprudence in the matter as exists. Where there is none, or no definite jurisdiction, it is based upon the general principles of Italian fiscal law and expresses the personal views of the author.

Accordingly, no absolute value can be attached to what will be said below. Account should also be taken of the fact that jurisprudence, though relatively stable in Italy, may always change.

A. FOREIGN ENTERPRISES.

1. DEFINITION AND GENERAL PRINCIPLES.

As already pointed out in Part I, a foreign enterprise, whether consisting of a single individual, a partnership or a company, is liable to tax on movable wealth in respect of income of all categories, on the one condition that that income is produced in Italy. Italian fiscal law being based upon the principle of absolute equality of treatment between Italian and foreign nationals, the Treasury assesses foreign enterprises for tax on movable wealth in virtue of the same rules that apply to the taxation of national enterprises. Likewise foreign enterprises enjoy the permanent or temporary exemptions granted to national enterprises. The only noteworthy exception to this rule is the temporary exemption from tax on movable wealth granted to income derived from merchant shipping built in Italy for Italian nationals (Article 5 of Royal Decree No. 211, of February 1st, 1923, and Article 8 of Royal Decree No. 865, of May 16th, 1926).

In order that a foreign enterprise may be assessable for tax on movable wealth, it must, we repeat, have in Italy a permanent productive organisation in the form of a branch, representative, agency, purchase and sales office, goods depot, manufacturing establishment or some other permanent organisation showing that the foreign enterprise has transferred a part of its activity to Italy with a view to its regular deployment in that country. Thus no tax is imposed when the foreign enterprise merely sends a representative (commercial traveller) to Italy solely for the purpose of visiting customers and taking or giving orders, unless such representative enters on behalf of the foreign enterprise into some authentic contract or executes any deed of a kind that is then copied into Italian mortgage registers; in that case, as mentioned in Part I, the income is taxable in Italy if it is derived from the operation for which the contract or deed in question was concluded.

Similarly, there is no ground for taxation when the foreign enterprise operates in Italy through an intermediary — that is to say, a “really autonomous agent” (professional canvasser, representative or broker, etc.) within the meaning given to this expression by the Fiscal Committee of the League of Nations.

The law makes one exception to the general rule that foreign enterprises are taxable in Italy in respect of income earned in the country by a permanent productive organisation. This exception is in favour of foreign shipping companies, which are exempted from tax, on condition that Italian companies are similarly exempted in the foreign country.

As already stated, Italy and the United States of America have concluded a convention mutually exempting their shipping companies, and the same exemption is provided for in double-taxation treaties with France, Belgium, Canada. Italy is negotiating with other countries to the same end.

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) DIVIDENDS.

A foreign enterprise in receipt of dividends distributed by an Italian company is in no case liable to tax on movable wealth, because, as pointed out in Part I, the tax has already been imposed on the net profits of the Italian company and, accordingly, any share of profits subsequently distributed to shareholders reaches them after the tax on movable wealth has been deducted. The shareholder cannot be taxed a second time, for there is at present no other tax in Italy — distinct from the tax on movable wealth — imposed upon profits distributed as dividends or bonuses or in the form of percentage shares (*tantièmes*) to managers and directors of the company.

(b) INTEREST.

It has already been mentioned that municipalities, provinces, legal entities and share companies are bound to declare to the Treasury, at the same time as their income from movable wealth, all interest on liabilities representing the service of debts contracted by them. They have to pay movable wealth tax on this interest, but can obtain refund from their creditors. It was also said that, if the interest referred to bonds issued since September 30th, 1926, by provinces, municipalities, corporations and share companies, it was exempt from the tax on movable wealth.

Accordingly, a foreign enterprise is never *directly* taxed on interest received in Italy by the associations referred to in the last paragraph, whether the enterprise has an organisation or business centre in Italy or not. In the absence of a contrary agreement between the parties, it can only be asked by its debtor to refund the tax the latter has paid on interest of this kind. In the case, however, of interest on bonds issued since September 30th, 1926, the foreign enterprise is under no further obligation to refund the tax to its debtors, because the income in question is exempt and the debtor will not have paid any tax on movable wealth.

If the foreign enterprise is in receipt in Italy of interest from companies other than share companies or from individuals engaged in industry, commerce or a professional occupation, the rules of collection differ according to whether the foreign undertaking does or does not have representatives in Italy.

If it has, interest is deducted from the gross income in Category B of the person or company paying the interest, and is assessed directly on the foreign enterprise.

If, however, the foreign enterprise has no representative in Italy, so that the interest cannot be directly assessed on the party receiving it, the interest is not deducted from the Category B income of the debtor, but is included in that income and taxed as Category B income, the debtor having the right to recover the tax from his creditor.

Lastly, as regards interest paid by credit institutions and savings banks, a distinction must be made according as the interest is on deposits in savings banks or cash deposits of a commercial character.

Interest on savings bank deposits is deducted from the gross income in Category B of the credit institution or savings bank, and taxed against it as Category A income, subject to its right of recovery from the depositors, even if the latter are domiciled abroad.

On the other hand, interest on commercial deposits and current accounts is deducted from the Category B income of the credit institution or savings bank. It is not, however, assessed against the debtor as Category A income, but is included in the Category B income of the creditor and directly assessed against the latter.

(c) ROYALTIES FOR USE OF PATENTS, COPYRIGHTS AND OTHER INCOME FROM PERSONAL PROPERTY.

(1) *Invention Patents.*

(i) The income from an invention may result from the manufacture of the patented article, whether directly by the inventor or by a company to which the inventor has licensed his patent.

In neither case is there, strictly speaking, any taxation of income derived from the patent. If, however, income arises from manufacture, that income is classed as Category B and taxed against the inventor (*entrepreneur*) or the company, according to the general rules for the assessment of movable wealth on income in this category.

Consequently, the income from manufacture is taxable in Italy, on condition that the inventor (*entrepreneur*) or the company operates within the country. If, therefore, the manufacture is in the hands of a foreign enterprise, the latter is only taxed in Italy if it has a productive organisation within the Kingdom, and taxation is limited to income derived from that organisation.

(ii) On the other hand, income from an invention patent may result from the granting by the inventor of a licence to third persons, authorising manufacture of the patented article on payment of a royalty.

These royalties are taxable as professional income (Category C1) in accordance with the general provisions for the assessment of this category of income for purposes of tax on movable wealth. If a foreign inventor is paid royalties on manufacturing licences granted by him in Italy, he is not liable to tax on movable wealth, because the income is regarded as earned in the State where the inventor is domiciled.

If an industrialist has bought an inventor's patent and in his turn grants manufacturing licences, the income therefrom is taxable as Category B income, along with the income derived from the exercise of his industry.

If a foreign enterprise, after acquiring an inventor's patent, receives royalties on licences granted in Italy, it is liable in respect of Category B income, if it has in Italy a permanent organisation enabling it to carry on the industry to which the patent refers.

(iii) Income from an invention patent may also arise from sale of the patent.

The price obtained by the original inventor for the sale of his patent is taxable as Category C1 income — *i.e.*, income derived exclusively from brain-work. Occasionally, however, the sale price may be regarded as Category B income; for instance, when an inventor, in order to realise his invention or discovery, has had to employ capital belonging to an industrial organisation. In the case of a foreign inventor who sells his patent in Italy, the price received is not liable to tax on movable wealth, because it counts as income earned in the seller's country of domicile, unless the sale is the outcome of a notarial deed executed in Italy.

If the person or company who sells the patent is professionally engaged in the buying or selling of patents, the price of these patents constitutes Category B income, on which the seller must pay tax.

When foreign individuals or companies sell their patents in Italy, the income from the sale is

liable to tax on movable wealth in Italy, but only if the seller has a permanent organisation within the country.

The last case to be considered is when an industrial enterprise sells a patent that belongs to it and appears among the assets of its business. The enterprise's profit on the sale is taxable as Category B income. It consists of the difference between the price the enterprise had to pay to acquire the patent and the higher price at which it sold it. If the industrial enterprise that sells the patent in Italy is a foreign enterprise, taxation is conditional upon its having a permanent organisation in the country or the sale being the result of a notarial deed executed in Italy.

(2) *Copyrights.*

Royalties on authors' works are taxable in Category C1 as professional income.

If a foreign author receives royalties in Italy, he is not liable to the tax on movable wealth, because the income cannot be deemed to have been produced in Italy, but rather in the country where the author is domiciled.

If the author has sold his rights, the income received from sale is taxable under Category C1, whether it consists of a lump sum or of a royalty paid annually or in respect of each copy sold.

If a foreign author sells his rights to an Italian publisher, he is not liable to tax on movable wealth in respect of the income resulting from the sale, unless the latter is the outcome of a notarial act executed within the Kingdom.

The person to whom copyrights are sold is taxed under Category B for the exploitation of those rights, but, if the purchaser is a foreign enterprise, taxation is, as usual, conditional upon the enterprise having a permanent organisation in Italy.

(3) *Personal Property.*

The rules applying to the taxation of income from movable wealth were explained above in connection with the taxation of dividends, interest and bank deposits.

A few words are needed about the taxes on business transactions to which a foreign enterprise is subject in Italy.

If a company has its seat abroad, but a branch or a representative in Italy, and if it issues shares and bonds abroad, these are subject to stamp duty at the rates given below, if they are negotiated in Italy or in any way utilised there.

On each sheet not exceeding 14 sq. dcm. in size, 3 lire ; exceeding 14 but not exceeding 20 sq. dcm., 5 lire ; exceeding 20 but not exceeding 30 sq. dcm., 7 lire ; exceeding 30, 15 lire.

Foreign companies with a branch or a representative in Italy are liable, in addition to the above stamp duty, to an annual payment of 4½ per thousand of capital set aside by them or actually used for operations in Italy.

If the company has no branch or representative in Italy, it is not taxed on capital set aside or used for operations within the country. But if the company's shares and bonds circulate or are in any way used in Italy, they are liable to a proportional stamp duty of 2.40 lire for each hundred lire, or part of a hundred lire, of the nominal value of each bond.

(d) RENTS FROM REAL ESTATE, MINING ROYALTIES AND SIMILAR INCOME.

(1) *Rents from Real Estate.*

As pointed out in Part I, income from real estate (except factories and rural houses) is liable to the taxes on land and buildings. This tax is imposed on real estate in Italy, whether the owners are nationals or foreigners.

If the land is leased, the owner, whether a foreigner or an Italian national, is required to pay land tax on the rent which represents the income (*reddito dominicale*).

If, however, the premises are used as *factories* or if the property consists of land industrially exploited as *mines, quarries, peat-bogs* or *salt-works*, tax on movable wealth under Category B is levied upon the rent paid to the owner by the person or company leasing the factory, mine, quarry, etc. This tax also applies to a foreign owner who lets on lease factories, mines, quarries, etc., owned by him in Italy.

(2) *Mining Royalties and Similar Income.*

Income from the industrial exploitation of mines is liable to tax on movable wealth (Category B). It is paid by the person, partnership or company carrying on the industry.

The income liable to tax includes the income from the land on which the mine is situated. (This was mentioned in Part I.) According to the law, the income from this land is not liable to the land tax, but counts as part of the income resulting from the working of the mine.

Accordingly, a distinction must be made between the exploitation of a mine directly by the owner and the leasing of the mine to another.

If it is worked directly by the owner, the question is simple, for he is liable to tax on income from movable wealth, Category B, in respect of the whole net income of his business, including income from the estate on which the mine is situated.

If, on the other hand, the mine is leased, the lessee who works the mine is liable to movable wealth tax on the net income he derives from his industry, the rent he pays to the owner being deducted from the gross income. This rent is assessed upon the owner, not as landed income, but as income from movable wealth, Category B, as was explained in reference to buildings used as factories and land worked as mines, quarries, peat-bogs or salt-works.

Foreign enterprises working mines in Italy are liable to movable wealth tax on the income from their mining industry. All foreign owners of mines in Italy are similarly liable on the rent they obtain from the lease of those mines.

(e) GAIN DERIVED FROM THE PURCHASE AND SALE OF REAL ESTATE AND SECURITIES.

(1) *Real Estate.*

The sale of real estate is governed by the following principle :

The profit from such sale is only liable to tax on movable wealth if the sale is in the nature of a speculation. The sale is judged to be speculative if business in real estate is an habitual activity of the persons concerned. Thus tax in respect of Category B income is levied upon all individuals and corporations habitually engaged in the purchase and sale of rural or urban estates or in the erection of buildings intended for sale. An isolated transaction may also be speculative; for instance, when a man acquires the whole of a building with the purpose of selling it again as flats or when he acquires a single flat, not for his own use, but with the intention of re-selling it. On the other hand, an owner who sells a house originally acquired for his own use is not liable.

Tax on income from movable wealth is payable by a foreign enterprise which makes a speculative business of buying and re-selling real estate in Italy. It is liable either because the object of its transactions is in Italian territory or because the profit is as a rule recorded in a notarial act executed in Italy or registered at Italian mortgage offices.

(2) *Securities.*

The sale of securities is not subject to the tax on income from movable wealth unless it is an act of speculation. Thus a shareholder who at any time sells his shares with a view to

reconstituting his fortune is not liable for tax on movable wealth. In order to be speculative, the buying and selling of securities must be the habitual activity of the person concerned. An isolated transaction may, however, be speculative, as when a taxpayer buys a block of shares and sells it at a higher price. In this case, the profit on the transaction is liable to tax on movable wealth.

The above principles apply both to individuals and to companies ; in the case of share companies, however, the Treasury normally assesses tax on the basis of the balance-sheet, in accordance with the system of alternate balance-sheets — a matter dealt with at some length in Part I.

The gain from speculative transactions in securities is taxed as Category B income, in the case of both individuals and companies, the income being of a commercial nature and produced by a combination of capital and personal activity.

A special word must be said about the taxation of income derived from speculation in securities by banks.

The purchase and sale of securities for speculative purposes are undoubtedly among the essential activities of banks. Moreover, banks may become the possessors of securities through participation in various industrial and commercial enterprises.

Accordingly, banks have at all times in their portfolios a certain quantity of securities which figure in the assets of the balance-sheet at a value varying from one balance-sheet to another according to Stock Exchange quotations.

Existing jurisprudence has decided that upward movements in the value of the banks' securities are not a ground for taxation, any more than downward movements justify a deduction from gross income, so long, that is to say, as the securities are not actually sold. Tax will only be imposed when the securities are sold and there is a gain or loss on the transaction.

In other words, the Treasury, when taxing the profits on speculative transactions in securities by banks, applies the same rules as to individuals and to other companies. Jurisprudence has refused to admit that a fall in the value of a bank's securities shall, of itself and apart from the sale of the securities, warrant a deduction from gross income on grounds of loss. The chief argument of the other side is that the securities of banks correspond to the goods of other companies. And since depreciation of goods is regarded as a loss and this loss may be deducted from gross income, although the goods are still in the possession of the company, so, it is claimed, the depreciation of securities should be balanced by an equivalent deduction from gross income, even when the securities have not left the bank's portfolios.

It is, however, established that, in the matter of speculation in securities, no matter on whose part, the Treasury, for purposes of tax on movable wealth, only considers actual gains and losses arising from the sale of the shares. It takes no account of fluctuations in the value of securities which the persons concerned continue to hold.

A foreign enterprise which engages in speculative transactions in Italian and foreign securities is only liable to tax on movable wealth if it has a permanent organisation in Italy. In the absence of such organisation, it is not liable on the mere ground that it has bought or sold securities in Italy.

(1) SALARIES, WAGES, COMMISSIONS AND OTHER REMUNERATION FOR SERVICES.

As regards income from labour, both intellectual and manual, the principle obtaining in Italy is that taxation is governed by the domicile of the person who furnishes the labour. Thus a foreigner is only liable to tax on movable wealth in Italy if he has acquired an Italian domicile. Further, he is only liable in respect of income derived from his activities in Italy, except as regards liability to complementary tax. The latter, as was pointed out in Part I, extends to income derived from activities abroad, if the income is received in Italy.

The same applies to foreign workmen in Italy, but, in this matter, the Italian administration exempts workmen's wages unless a man is discharging special or confidential duties of a permanent kind.

All the above applies, of course, to individuals working on their own account.

As regards individuals working for an enterprise, the tax on salaries and wages is due by the enterprise which pays the income in question, subject to its right of recovery. Accordingly, foreign enterprises have to pay (subject to recovery) tax on movable wealth in respect of income paid out as salaries and wages to employees and workmen attached to a permanent organisation of the enterprise in Italy. Even in this case, taxation in practice touches only the wages of workmen who are engaged in special or confidential duties of a permanent kind.

(g) INCOME FROM A TRUST.

First, let it be observed, the trust as known in Anglo-Saxon law does not exist in Italian law and there is no Italian jurisprudence in the matter of trust taxation. What follows concerning "trusts" in the sense of holding companies, or a fusion of commercial companies is therefore in the main the opinion of the writer of this report, based on the general principles of Italian fiscal law and on the jurisprudence followed in similar cases.

Next, a distinction must be made between two cases: (1) when the trust is simply the concentration of blocks of shares of different enterprises, the latter preserving their separate legal entity; (2) when the trust represents a fusion of different enterprises into a single concern such that those enterprises lose their own legal individuality, which is merged in that of the trust. On the supposition that the seat of the trust is in Italy, and taking the first case, the various enterprises in the group are liable to tax in respect of the income earned by each of them — this in virtue of provisions common to all enterprises, whether trusts or not. If, therefore, there are foreign enterprises belonging to the trust, these can only be taxed on income earned in Italy if they have a permanent organisation there.

The trust, however, even if it is not a legally constituted company, can still be regarded as an organisation carrying on activities of its own in accordance with the purposes assigned to it by the participating enterprises. A trust, therefore, is in principle liable to tax on movable wealth in respect of all receipts of any kind resulting from the exercise of those activities. Before defining the nature of these receipts or gains or how and to what extent they can be assessed, we must await the establishment of jurisprudence on the subject.

Taking the second case, that in which the trust constitutes an enterprise with an independent legal existence, such a trust will be subject to tax on movable wealth in respect of all income resulting from the exercise of its activities. But, as any foreign enterprises belonging to the trust would in the end become so many branches of a trust with its seat in Italy, the provisions of Article 9 of the Royal Decree dated August 12th, 1927, might apply. This article exempts from tax on movable wealth the income which an enterprise with its seat in Italy derives from its branches abroad, when the accounts of those branches are separate from the accounts of the central seat.

(h) INCOME FROM THE CARRYING-ON OF A BUSINESS OR INDUSTRY THROUGH :

- (1) A local commission agent or broker ;
- (2) A commercial traveller ;
- (3) An agent with a power of attorney ;
- (4) An agent selling out of a stock belonging to the foreign enterprise ;
- (5) A permanent establishment.

As several times mentioned, a foreign enterprise is only liable to the tax on movable wealth in respect of income from operations in Italy, if it has in Italy a permanent organisation through which it operates permanently and continuously.

This organisation, as has also been said, may be a branch, agency, representative, goods depot, purchase and sales office, establishment for the sale or working up of products or, finally, any

industrial or commercial organisation proving that the foreign enterprise has transferred part of its productive activity to Italy with a view to its more or less permanent exercise there.

If, therefore, a foreign enterprise operates in Italy through a *commission agent*, it is not liable for tax on movable property, because such agent works in his own name and cannot be regarded as directly forming part of the foreign enterprise. Moreover, the separate income of this commission agent is itself liable to the tax, since he is a trader carrying on business in Italy. The same may be said to apply if the foreign enterprise operates through a *commercial traveller*, who comes to Italy for the sole purpose of visiting customers to give and take orders. Periodical visits to Italy of a commercial traveller do not amount to a permanent establishment. According to modern jurisprudence, not even the earnings of the commercial traveller are liable to tax on movable property, it being held that the seat of his business is in the country of which he is a national.

The same may be said of a foreign enterprise operated through an *intermediary* (broker), for a *bona-fide* intermediary remains a factor extraneous to the foreign enterprise. All he does is to establish contact between the enterprise and Italian customers and he then leaves it to the former to deal directly with the latter. The only liability to tax on movable property is in respect of the broker's earnings from his activities.

On the other hand, if the foreign enterprise operates through an *agent having a general power of attorney*, the enterprise is subject to the tax on movable property in the name of that agent, who is regarded as a permanent representative of the foreign undertaking with powers to act on its behalf and in its interests.

In the case of an *agent with special power of attorney* responsible for carrying through a specific transaction for and on behalf of the foreign enterprise, the latter does not become liable to the tax on income from movable property by reason of the activities of this special agent. The power of attorney covers a single act and does not imply the existence of a permanent organisation of the foreign enterprise in Italy.

Moreover, both the agent with general and the agent with special power of attorney are liable to the tax on income from movable property in respect of the income they themselves derive from the exercise of their power of attorney.

In the same way as when it operates through an agent with a general power of attorney, the foreign enterprise is liable if it operates through an *agent whom it employs to sell goods in its possession in Italy*. As mentioned above, a goods depot constitutes a permanent organisation, whatever may be the method of selling the goods.

Even in the absence of a general power of attorney or goods depot, if the foreign enterprise maintains in Italy one or more agents depending upon it and qualifiable as employees (not intermediaries really autonomous in the sense given to this term by the Fiscal Committee of the League), the Treasury will regard the foreign enterprise as having a permanent establishment in Italy.

B. NATIONAL ENTERPRISES.

1. DEFINITION AND GENERAL PRINCIPLES.

The answer to this question necessitates distinguishing between two cases : (1) when the enterprise has its effective centre in Italy and operates abroad without having a branch abroad with its own separate accounts, and (2) when the enterprise has a foreign branch whose accounts are distinct from those of the central seat.

In the former case, the enterprise is liable for tax in respect of its total net income from movable property, including income from its foreign operations which goes to make up the total income of the enterprise. The assessment of this total income is governed by the usual principles, it being understood that, if the enterprise is a share company, the Treasury normally takes as its basis the information, duly checked, in the balance-sheet. In the cases of enterprises other than share

companies, total income is assessed on the financial results of the two preceding years, these results being determined in the light of all available information.

For the rest, the tax on income earned abroad is merged in the total tax due from the enterprise ; it is collected at the same time as the latter and without being distinguished from it, according to the general rules for collection.

In case (2) above — *i.e.*, when the enterprise operates abroad through branches with separate accounts — the income from the foreign activities of the branch is exempt from tax on movable property.

It then becomes necessary to determine the exact income to be ascribed to the branch. Means must be taken to prevent a part of the income of the central seat from being fraudulently assigned to the branch. For this purpose, the law requires the enterprise to submit to the revenue authorities the separate accounts of the branch with all the evidence necessary to prove the actual existence of the branch's income. The revenue authorities check the accounts of the branch, comparing them, if necessary, with those of the central seat. They fix the income to be ascribed to the branch and exempted from tax on similar lines to those they would follow in order to determine the taxable income of a branch owned by a foreign enterprise in Italy.

Following these general explanations, we may now examine the taxation of the different kinds of income which an Italian enterprise may derive from abroad.

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) and (b) DIVIDENDS AND INTEREST.

These can be taken together, the same rules applying to both.

Dividends and interest received by a private taxpayer from the shares and bonds of a foreign company are exempt from tax on movable property, because the Treasury, as regards individuals, considers the holding of these securities to represent a non-speculative investment of a part of their property abroad. Consequently, the dividends and interest constitute income produced outside Italy.

The same cannot apply to dividends and interest received by an industrial or commercial enterprise from the shares and bonds of foreign companies in its portfolio. In the case of these enterprises, the possession of foreign securities implies the pursuit of speculative aims as an essential characteristic of the enterprise. They are therefore part of the company's speculative activities.

It would seem to follow that dividends and interest from the securities of foreign companies are not in and by themselves taxable as Category A income against an industrial or commercial enterprise having its seat in Italy. Instead, they should join Category B and, along with the other elements of that group, make up the total net income on which the enterprise is liable for tax. In other words, they should contribute towards the total net income from the exercise of industry or commerce.

And jurisprudence has, in fact, decided in this sense, though with some uncertainty. The question is keenly disputed, and the solution here offered must not be regarded as absolute or final, since jurisprudence may change with time.

The principles set forth above apply also to income which an Italian company derives from shares in a foreign subsidiary. In this matter, however, the financial administration has allowed that, in certain cases, the income obtained from the possession of all or a substantial majority of the shares of a subsidiary shall be exempt from tax on movable property. Thus the administration extends to this income the clause exempting from tax the income of branches having their own separate accounts.

(c) ROYALTIES FOR USE OF PATENTS AND COPYRIGHTS AND OTHER INCOME DERIVED FROM PERSONAL PROPERTY.

An inventor resident in Italy has to pay tax on movable wealth in respect both of the income from the sale of his patent abroad and of income from licences granted in other countries for the manufacture of the patented article.

In principle, the tax falls on Category C1 income but, occasionally, may be levied under Category B, if the inventor, in order to realise his invention, has employed capital and an industrial organisation.

As regards authors' copyrights, an author resident in Italy is liable to Category C1 tax in respect of his receipts from the sale of his rights in other countries. If the inventor or author has contributed his patent or literary work to a foreign industrial enterprise for exploitation, the fraction of the enterprise's net income accruing to the inventor or author would be exempt from tax on movable wealth, the Treasury holding that such income is produced in the State where the enterprise has its seat.

As regards income from other movable wealth, reference may be made to what was said above in connection with dividends and interest.

(d) RENTS FROM REAL ESTATE, MINING ROYALTIES AND SIMILAR INCOME.

In Italy, real estate taxes (taxes on land and buildings) do not touch the income which an enterprise with its seat in Italy derives from the lease of its immovable property abroad. Nor is this income included in the income on which the enterprise is assessed for tax on movable wealth.

The same applies to income from the leasing of mines, quarries, peat-bogs and salt-works owned abroad by an enterprise whose effective seat is in Italy.

If an enterprise with its seat in Italy has a participating share in a mine abroad, the receipts from that participation contribute to make up the income liable to tax on movable wealth. In this case, the principles to be applied are those set forth in regard to income from shares in foreign companies.

(e) GAIN DERIVED FROM THE PURCHASE AND SALE OF REAL ESTATE AND SECURITIES.

If an enterprise seated in Italy engages in profit-making transactions for the purchase and sale of real estate abroad, it is liable to tax on movable wealth in respect of the gain from these transactions, while also paying tax on its gains from profit-seeking transactions in the purchase and sale of real estate in Italy. Here, again, the general principle applies whereby all enterprises are liable to tax on movable wealth, provided their effective seat is in Italy, even if the income is derived from industrial and commercial activities abroad.

On the other hand, the enterprise will be exempt from this tax if the foreign business is transacted by a branch with entirely separate accounts.

If an enterprise whose effective seat is in Italy derives gain from foreign transactions in securities and if these transactions have a profit-making purpose, such gain is liable to tax on movable wealth. This gain may be regarded as produced in the country where the enterprise owning the securities has its seat.

(f) SALARIES, WAGES, COMMISSIONS AND OTHER REMUNERATION FOR SERVICES.

As already mentioned, income from labour, both intellectual and manual, is taxed in the place where the labour is performed. Accordingly, an Italian national is not liable to tax on movable wealth in respect of income resulting from activities deployed abroad, whether these are professional or simple manual labour, apart from the special regulations concerning the application of complementary tax. The above rule applies only to individuals working on their own. In the case of persons working for an enterprise, the tax on salaries and wages is due from the enterprise that pays the income, subject to its right to recover from the persons concerned.

In principle, enterprises with their seat in Italy would be required, subject to right of recovery, to pay tax on movable wealth in respect of the salaries of their employees employed abroad, with the exception of the employees and workmen of a foreign branch with separate accounts. In practice, however, the Treasury, even when there is no branch with separate accounts, often refrains from taxing the salaries of employees working abroad, especially when they are locally recruited.

(g) INCOME FROM A TRUST.

When examining (on page 265) the taxation of income from a "trust" with its seat in Italy, a distinction was made between two cases. When the trust has its seat abroad, two cases also arise: one in which the trust does not acquire legal personality, but represents a mere concentration of enterprises which retain their own legal individuality; the other in which the trust constitutes an organ having a legal existence of its own and resulting from the complete fusion of the different enterprises.

In the former case, taxation is governed by the general provisions applying to all enterprises having their seat in Italy and belonging to the trust, and there is no need to take account of the internal relations between those enterprises and the management of the trust.

In the other case, enterprises with their seat in Italy end by becoming permanent organisations operating in Italy as branches of the foreign trust; and the latter will be taxed in the name of its organisation in Italy and on the whole net income earned in Italian territory, according to the general rules and principles governing the taxation of all permanent organisations in Italy owned by foreign enterprises.

(h) INCOME FROM THE CARRYING-ON OF A BUSINESS OR INDUSTRY THROUGH:

- (1) A commission agent or broker;
- (2) A commercial traveller;
- (3) An agent with power of attorney;
- (4) An agent selling out of a stock belonging to the foreign enterprise;
- (5) A permanent establishment of any kind.

In connection with the taxation of profits derived by an Italian enterprise from transactions effected abroad, we must distinguish according to whether an enterprise with its seat in Italy operates abroad through a *commission agent*, *intermediary* or *commercial traveller* or whether through an *agent directly dependent upon the enterprise*, with or without power of attorney, or through a *permanent organisation*.

In the first case, the enterprise is liable on all income derived from abroad, in accordance with the principle that, in matters of taxation, the Treasury takes no account of where the various operations are effected, but only of the place where the enterprise has its centre of activity. It is not possible to apply to this case the legal exemption from tax of the income of foreign branches with separate accounts. A *commission agent* and a *broker* (intermediary) do business on their own and are not in a relation of dependence upon the enterprise; their activities therefore cannot be assimilated to those of a branch. Nor can a *commercial traveller's* business be compared with that of a branch, since he is not permanently established in the foreign country, but only visits customers from time to time to give or receive orders.

In the second case, however, when the enterprise maintains in a foreign country an *agent of its own* responsible for doing business on behalf of the enterprise (with or without power of attorney), the representative in question can be assimilated to a branch of the undertaking. Consequently, the legal provision exempting from tax the income of foreign branches of the enterprise can be applied, granted, of course, fulfilment of the condition imposing upon branches accounts entirely separate from those of the central seat.

The same principles apply when an enterprise whose seat is in Italy has a permanent establishment abroad, whatever, moreover, are the activities of that establishment.

PART III. — METHODS OF ALLOCATING TAXABLE INCOME

A. FOREIGN ENTERPRISES WITH LOCAL BRANCHES OR SUBSIDIARIES.

I. GENERAL QUESTIONS AND METHODS OF APPORTIONMENT.

(a) BOOK-KEEPING AND ACCOUNTING REQUIREMENTS.

Italian fiscal law contains no provision obliging enterprises to keep special accounts for the purpose of assessing taxable income. The financial administration therefore makes use of the accounts and documents which traders are required to keep by the general provisions of the Commercial Code.

Articles 21 *et seq.* of the Commercial Code lay down that every trader must keep a day-book in which all his business transactions without exception are entered day by day, together with his receipts and expenditure of whatever kind, and this independently of the fact that he may keep other commercial books, the use of which, while not compulsory, is usual in business. He must also keep in file the letters and telegrams he receives and copy the letters and telegrams he sends out.

Further, every trader has to prepare an annual inventory of his movable and immovable property and of his debts and claims, whatever their nature and origin, and this must be transcribed in a special register.

The inventory is closed at the same time as the annual balance-sheet and the profit-and-loss account, and is used for the preparation of these two documents.

The profit-and-loss account constitutes the essential document for the determination of the taxable income of commercial companies and, in particular, of share companies, for which, as it has already been pointed out above, such determination must be made as a rule on the basis of the balance-sheet.

The revenue authorities can, of course, make use of any other books and registers kept by the trader over and above those prescribed by the Commercial Code.

They may also require the taxpayer to produce any extracts or documents they may need in order to fix the exact taxable income.

If the taxpayer refuses to produce his registers and to furnish the extracts and documents asked for, Italian fiscal law has no means of compelling him to do so ; in such case, however, the revenue authorities will assess the taxable income in a presumptive manner on the basis of the information at their disposal.

It will then rest with the taxpayer to prove that the income as fixed by the authorities is not in accordance with the facts.

(b) METHODS OF ALLOCATION.

Italian law on the movable wealth tax contains no provisions for assessing by any particular method the income earned in Italy by the branch of a foreign undertaking in Italy or by an Italian company affiliated to a foreign company.

It has already been mentioned in the course of this report that Italian fiscal law is based upon the principle of perfect equality of treatment between nationals and foreigners. Consequently, in applying tax on movable wealth, the law has exclusive regard for the production of that income and tries to assess it as exactly as possible for all taxpayers liable towards the Italian State for this tax. It makes no distinction between Italian taxpayers and foreign taxpayers, between companies with an entirely independent existence and companies affiliated to other Italian or foreign companies or between enterprises operating on their own account and enterprises operating as branches of enterprises founded abroad.

The law lays down no special method of determining the taxable income of branches or subsidiaries of foreign enterprises. Resort must therefore be had to the general rules for fixing the taxable income of all other enterprises operating in Italy.

A branch of a private enterprise is required to declare its income to the revenue authorities under the provisions referred to in Part I of this report. The authorities then examine and check the declaration and for the purpose exercise the powers and avail themselves of the sources of information likewise mentioned in that part of the report.

In order better to test the returns of the branch or, in the absence of a return, in order to assess at their own discretion, the authorities may also compare the activities of the branch with those of other enterprises engaged in the same line of industry or commerce. A comparison of one enterprise with all others of the same kind is a most important means of estimating the exact taxable income. The Treasury not only uses this method for testing the declarations of income by branches of foreign enterprises, but regularly employs it, among other methods, in determining the taxable income of national enterprises.

In the case of branches or subsidiaries of *foreign companies*, the revenue authorities may assess income on the balance-sheet of the branch or subsidiary, which both are required to publish under Article 230 of the Italian Commercial Code.

In checking the balance-sheet of branches or subsidiaries, the Treasury observes the general principles set forth in Part I and has recourse, among other expedients, to the comparative method. As regards subsidiaries, this method is of particular importance, inasmuch as it can, for example, help to determine the exact price of goods and products which the subsidiary acquires from the parent company with a view to selling them again in Italy.

It will not be possible to apply the method of comparison if, as is very unlikely, the branch or subsidiary of the foreign enterprise engages in activities differing from those of any other enterprise. In this case, the revenue authorities with the greatest care collect all possible information or data that can help to determine the income. The branch or subsidiary, on the other hand, like all other taxpayers, retains the right to claim a reduction of its quota if it can show that the income figure declared by the administration does not correspond to the facts, producing for this purpose all relevant evidence before the revenue office itself or before the administrative committees appointed to decide on fiscal disputes.

Lastly, the Italian Treasury respects the separate legal existence of subsidiaries and, in assessing income, takes exclusive account of the latter's operations.

Having offered these explanations, we may now examine each of the different methods of allocation.

I. *Method of Separate Accounting.*

The rule is that the income of the branch must be determined separately, as if it were an enterprise completely independent of the parent company abroad.

The revenue authorities, as already mentioned, may resort to any means at their disposal ; in the main they seek to eliminate all possibility of confusion between branch and central seat and any transfer of gains or losses from the accounts of the one to those of the other. In order to arrive at these results, the law, as stated, lays down no special rule for determining the taxable income to be ascribed to the branch. It rests therefore with the revenue authorities to collect all the available data calculated to show the real nature of the income taxable against a branch in Italy.

2. *Empirical Methods.*

Italian law has no empirical method of determining the taxable income of a branch or subsidiary of a foreign enterprise. Nor has it any similar method for determining the taxable income of Italian enterprises.

In certain cases, however, the Treasury does, in practice, adopt methods that may be called empirical. If it does so, it is as a result of agreements between its representatives and the representatives of trade-union organisations or associations of various categories of taxpayers. These agreements are also valid for branches and subsidiaries of foreign enterprises, but more will be said of them later (pages 277 and 278).

3. *Method of Fractional Apportionment.*

It is clear from the foregoing that, in order to determine the taxable income of a subsidiary or branch of a foreign enterprise, Italian law will in no case regard this income as a fraction of the total income of the parent company. The law rests on the principle that the object of determination is to ascertain the amount of income actually produced in Italy by the branch or subsidiary, apart from the total income earned by the parent company operating on its own account abroad.

4. *Requirements for Selection of Methods and Value of the Various Methods.*

The only method employed by the Italian Treasury is that of separate accounting. This method, which aims at determining the exact income earned in Italy, is in harmony with the principle of the *territoriality* of income. More than that, it saves having to determine the total income of the entire enterprise through all its various operations and activities in different countries. It is difficult enough to determine this total income, but it is even harder to allocate it between the centre of management and the various organisations (branches and subsidiaries) abroad.

(c) APPORTIONMENT BETWEEN BRANCH AND PARENT ENTERPRISE.

1. *Apportionment of Gross Profits of Local Branch to Real Centre of Management abroad.*

Italian law does not allow a fraction of the net income earned in Italy by a subsidiary or branch to be ascribed to the centre of management abroad and thus escape taxation in the Kingdom. In determining a branch's net income, however, the Treasury does in practice allow a certain deduction for "general overhead", representing the activities of management and the expenses of the centre of management.

2. *Apportionment of Expenses of Real Centre of Management to Branch or Subsidiary.*

Interest Charges. — It is the custom to distinguish between subsidiaries of a foreign enterprise and branches. As regards the former, there can be no possibility of ascribing to the subsidiary a portion of the debts contracted by the parent company. The subsidiary has an independent legal existence and the Treasury can only take into account debts it has contracted in its own name.

In the case, however, of a branch or other organisation, it must be noted that, should a fraction of the debt contracted by the parent company be ascribed to the branch, the interest on that part of the debt could not be deducted from the gross income (Category B) accruing to the branch. The reason for this is that, as was pointed out in Part I in connection with annual charges on liabilities, the law makes deduction conditional upon the name of the creditor being known and the creditor himself having an Italian domicile.

Nevertheless, when the Treasury determines in practice the general overhead to be deducted, if necessary, from the gross income of the branch, the administration may possibly take account, in one form or another, of the return on the interest on money borrowed by the parent company in order to organise the Italian branch.

Overhead Expenses. —As regards subsidiaries, none of the overhead expenses of the parent can be attributed to the subsidiary; the reason of this is the same as the one set forth in connection with interest. As regards the apportionment of general overhead between the parent enterprise and its branch, it must first of all be observed that, wherever there is an exchange of goods, products, raw materials, etc., between parent company and branch, a fraction of general overhead will generally be found to be included in the price of these articles. In such cases, the only duty of the revenue authorities is to check the declared price in the light of all available information in order to ascertain whether it corresponds to the current price, which already includes general overhead.

If there is no exchange of goods, products or raw materials between parent company and branch, the law has no precise rules for the apportionment of general overhead, but the revenue authorities settle each case in proportion to the size of the branch's business. In practice, the fraction of general overhead to be ascribed to the branch will generally be included in a round sum, which will include all the expenses to be deducted from the gross income of the branch.

3. *Apportionment of Net Profits.*

Of Branch to Deficitary Parent. — The Italian tax on movable wealth being based on the principle of the territoriality of income, Italian law looks only to the income earned in Italy by the branch or subsidiary of the foreign enterprise. It assesses this income for tax without regard to the results of the foreign enterprise's direct activities or of its activities through all its branches and subsidiaries. Consequently, if this total result is a deficit, that deficit does not affect the taxation of the income earned by the subsidiary or branch in Italy.

Of Parent to Deficitary Branch. — If the accounts of the branch or subsidiary of a foreign enterprise show a deficit, the principle of territoriality ensures that such branch or subsidiary does not have to pay tax on movable wealth, even if the total activities of the foreign enterprise, both direct and through its various branches and subsidiaries, result in a profit.

Further, even in the event of a deficit, the branch or subsidiary has to pay the tax on all the salaries and other remunerations of the agents it employs (Category C2 income). In this case, tax is payable by the branch or subsidiary, but the latter may recover it from their employees or workmen.

(d) APPORTIONMENT BETWEEN PARENT ENTERPRISE AND SUBSIDIARIES.

In the case of the income of a subsidiary company, the Treasury determines it separately, as if it were an entirely independent company. If the subsidiary is a share company, it is subject to the same rules as all other share companies whose seats are in Italy. Determination is then based upon the subsidiary's balance-sheet, which is the main piece of evidence in taxing companies of this kind.

The revenue office, however, has the right to check the balance-sheets of all companies having their seats in Italy, and therefore those of subsidiaries of foreign companies. It can thus remove

from the liabilities all items which fiscal law does not allow to be deducted from gross income (taxes and contributions, for instance); it can also correct any items in the balance-sheet which may not appear to conform to facts and thus may falsify the final result.

For this purpose, the revenue authorities may exercise the general powers conferred by the law, such as the power to inspect registers and demand all documents and explanations calculated to reveal the facts. Thus, they can demand to see the general accounts of the parent company. By these means, the authorities reconstitute the balance-sheet in accordance with fiscal principles and to this end may make use of the reports of the board of management and of the auditors and the minutes of the general meeting of shareholders. If necessary, they have the further right to audit the accounts.

It may happen that the company refuses to furnish the authorities with the documents and information necessary for checking the balance-sheet. It may also happen that the balance-sheet may not be drawn up in such a way as to supply a suitable basis for determination. In that case, the revenue authorities apply the general rule already mentioned, which authorises them to disregard the balance-sheet. They may then proceed on the presumptive method, as in the case of a private individual, and determine the taxable income of the subsidiary in the light of all available evidence.

II. APPLICATION OF THE METHODS OF ALLOCATION IN SPECIFIC CASES.

(a) INDUSTRIAL AND COMMERCIAL ENTERPRISES.

I. *Selling Establishments.*

Local Establishments selling in National Market. — As already stated, Italian law knows no special method of determining the income of a subsidiary or branch of a foreign enterprise in Italy. Its purpose is to assess for movable wealth tax the whole income which taxpayers earn in Italy, without any regard to the activities which create this income or the forms of these activities.

Consequently, if an enterprise manufacturing or buying abroad also sells in Italy through a permanent organisation established in the country, the tax on movable wealth is applied to the whole net income from these sales. But as, in this case, the sales in Italy are in respect of goods and products manufactured or bought abroad, the revenue authorities, when calculating the profit on these sales, are bound of course to ascertain as exactly as possible the cost of the foreign product sold in Italy. They will therefore employ every means in their power to determine this price and will then deduct all the expenses involved in the exercise of the trade in question. They will adopt this procedure, not only in the case of a permanent organisation established in Italy by a foreign enterprise, but as regards any Italian trader selling in Italy goods bought abroad.

In the special case of an organisation belonging to a foreign enterprise and selling in Italy, the revenue authorities may find it necessary to check very carefully the price at which the parent company invoiced its own products when supplying them to its Italian organisations, for they have to determine whether this price corresponds to current market prices. If the goods are such as have a universally known price, this process of checking will be quite easy, but for other articles the authorities will have to obtain the necessary data where they best can.

Still, it may be repeated, these various operations do not constitute a special method of assessment; they are merely part and parcel of the complex and detailed activities which the revenue authorities have to pursue in order to determine in each particular case the income of the different taxpayers.

Local Establishments selling abroad. — When an Italian branch sells in other countries the products of the foreign enterprise on which it is dependent, it is liable to tax on movable property in respect of that portion of the income from sales which is to be regarded as the result of its own separate activities. The fact that the foreign enterprise has created a branch in Italy for sale in third countries would seem to show that the enterprise has thought it necessary, or anyhow useful

for its purposes, to transfer a part of its commercial activities to Italian soil. It is therefore natural that the receipts obtained by the foreign enterprise from its permanent organisation in Italy should not only be taxed, but taxed to the account of the Italian organisation.

2. *Manufacturing Establishments.*

A foreign enterprise which has an establishment in Italy for the manufacture of products which it then sells abroad is liable to tax on movable wealth in respect only of the income from manufacturing in Italy ; this income consists of the difference between the cost price of the product and its price when it leaves the factory to be put on sale (wholesale price).

In addition to all other sources of information for determining this income, the revenue authorities may institute comparisons with other enterprises manufacturing the same article.

3. *Buying Establishments.*

Provided that it possesses no permanent organisation in Italy, a foreign enterprise is not liable to tax on movable wealth when it buys raw materials from other enterprises in Italy with a view to working them up and selling the products in other countries.

As regards the taxation of buying offices, jurisprudence is not very clear. Each decision taken reflects the actual circumstances of the particular case and the various activities of the particular office.

Speaking generally, however, the income taxable in Italy is the saving which the enterprise effects on the current market price it would have to pay for the finished product in Italy. In the cases with which we are dealing, the foreign enterprise obtains a cost lower than the market price, thanks to the activities of the buying office and in spite of the cost of organising that office.

Very often buying offices engage in various operations of sorting, classifying, making-up, etc., with a view to improving their products in the eyes of their customers in the country where they are sold. These operations which precede commercial operations proper are a source of gain which may be considered as earned in Italy. In a certain sense, these gains may be assimilated to the income to be ascribed to enterprises manufacturing in Italy for sale abroad. They represent the difference between the cost of giving the article its necessary make-up and the market price of the same product already so made up and ready for export. These gains are therefore taxable in Italy.

4. *Statistical Establishments, Display Rooms.*

When a foreign enterprise has an establishment in Italy which does not directly engage in profitable business but renders certain services to the enterprise, it is necessary to examine in each case how the Italian establishment is organised, how it functions and the real extent of its contribution to the productive activities of the foreign enterprise.

Keeping to the two examples quoted above, let us take the case of a statistical office responsible for collecting general data and information necessary for purely scientific economic research or as a guide to the industrial and commercial work of the foreign enterprise, such statistical office not being connected with a sales organisation in Italy. In such a case, the foreign enterprise and, through it, the statistical office are not liable to any tax on movable wealth. The office does not, in fact, constitute a productive organisation capable of earning income in Italy.

If, on the other hand, the statistical office is attached to a sales organisation in Italy established by the foreign enterprise, the income on which this organisation will be liable is larger or smaller according to the size of the receipts corresponding to the services rendered by the statistical office. There can be no separate taxation of the indirect receipts which the statistical office earns for the enterprise.

As regards display rooms, tax on movable property is not applied if the room simply makes known the goods of the foreign enterprise and does not take orders.

If, however, the display room takes orders from Italian customers and passes them on to the foreign enterprise, it must be regarded as a permanent organisation representing the enterprise. In this case, the Treasury will tax the income which the enterprise itself earns in Italy through sales arising out of orders secured by the display room from Italian customers.

(b) OTHER KINDS OF ENTERPRISES.

As mentioned several times, the Italian law governing tax on movable wealth follows the principle of full equality of treatment as between Italian nationals and foreigners. This equality applies, not only to the substance — *i.e.*, the assessment of the tax — but also to the form — that is, the method used to determine the exact income liable to the tax and the procedure for settling disputes between taxpayers and the Treasury concerning the determination of taxable income.

The principle of equal treatment for nationals and foreigners is general and absolute, and admits of no exceptions due to the nature of the activities from which the income results.

Accordingly, permanent organisations of foreign enterprises dealing in Italy in credit, insurance, transport and all the other special industries, are liable to tax on movable wealth exactly to the same extent as all national enterprises. The law has no special method for determining the taxable income of these organisations.

It merely instructs the revenue authorities to determine this income by the exercise of all the powers conferred upon them and by whatever means may seem in each particular case most likely to furnish an accurate estimate of the taxable income. On the other hand, the taxpayer will always have the right to appeal to the law and, in particular, to apply to the Committees of Direct Taxation and the judicial authorities within the limits and forms prescribed by law.

The problem therefore resolves itself into determining what are the chief sources of evidence and information to guide the revenue authorities in determining the taxable income of organisations permanently established in Italy by foreign enterprises.

Before, however, considering these factors, a digression may be allowed for the purpose of giving a short general account of certain practical methods in current use by the Italian Treasury for determining income.

In the first place, the net income of all enterprises can be determined by the use of an average figure (*chiffre forfaitaire*). This method is in contrast with analytical determination, which consists in determining the different items among the assets, and the liabilities corresponding to each of them. The method of average assessment (which is not compulsory for any given enterprise) presupposes agreement between the revenue authorities and taxpayers; both parties, however, may claim determination by an analysis of assets and liabilities.

In the case of share companies, the Treasury usually employs the balance-sheet method, as several times explained in this report.

There is, however, nothing to prevent net income from being determined by an agreement on the basis of a flat rate.

In some circumstances, income is determined from turnover, but the law in no case obliges the taxable income to be fixed on that basis, which is only one factor of assessment. Quite often, however, the revenue authorities and the taxpayer decide between themselves to take the turnover figure as the one basis of comparison for determining income, fixing the latter as a certain percentage of the actual turnover.

These agreements between the revenue authorities and the taxpayer are a very common practice in Italy. They allow the total taxable income to be fixed without gross income having first to be determined and without having to deduct the various liabilities. Before concluding the agreement, the authorities of course check the balance-sheet and obtain all the necessary data for determining income analytically. In this way, they are able to see how closely the taxpayer's figure

approximates to that resulting from the checking of the balance-sheet and the other evidence obtained.

In Italy, the proportion of cases determined by agreement is fairly high. It often amounts to 50 and even 75 per cent.

Apart from individual agreements between the revenue authorities and the taxpayer, general agreements are sometimes concluded between representatives of the administration and representatives of the various associations in which the different classes of taxpayer are grouped.

The purpose of these general agreements is to lay down the principles for determining the income upon which individual taxpayers are to be assessed.

This method of general agreements between the representatives of the administration and those of the taxpayers' associations was reinforced by the Law of April 3rd, 1926. This law has proclaimed the juridical existence of trade-union organisations and thus enabled their exact relations with the administration to be made clear and has provided that associations may be recognised as representing, in relation to the Treasury, the joint interests of a whole class of taxpayers, instead of the separate interests of individual taxpayers of that class. The method of general agreements is in perfect accord with this principle, for it establishes the rules for determining the income of a whole class of taxpayers without proceeding to determine the actual taxable income of each particular taxpayer. The latter is a matter for arrangement between the revenue office and each taxpayer, but the arrangement is based on general principles laid down in the agreement concluded with the competent trade-union association.

Agreements of this kind have been concluded for the purposes of determining :

- (a) Income from agricultural rents, a figure based upon a fixed percentage of the rent ;
- (b) Income from dairy work, which is based upon the quantity of milk treated, the tax being fixed at a given number of lire per 100 kilogrammes of milk treated ;
- (c) Income from the silk-weaving industry, etc., based on the number of looms at work, the tax being fixed at so many lire per loom ;
- (d) Income from the naval armament industry, based on different rules according to whether the vessel is a steamer or sailing vessel ;
- (e) Income from the salt-marsh industry ;
- (f) The abatements for depreciation and wear-and-tear of plant and movable material to be allowed as deductions from the gross revenue of railways and tramways ; amortisation deductions from the revenue of railways and tramways conceded to private enterprises, accompanied by an obligation to surrender the ownership of plant and material to the conceding party on expiry of the concession, without claim to compensation ;
- (g) In other numerous cases that need not be specified.

The method of general agreements between the Administration of Direct Taxes and the various trade-union associations will be still more widely used in the future, having been warmly welcomed by both parties. The great majority of taxpayers are equally in favour of it ; it saves them lengthy discussions with the revenue authorities and no less lengthy proceedings before the competent courts and committees.

The question at issue can now be answered in sufficient detail. First, one preliminary observation on the taxation of the organisations contemplated by the question — namely, Italian organisations belonging to foreign enterprises. The point of departure for this taxation is the balance-sheet, which these different organisations are required to keep in respect of their business in Italy. The question therefore resolves itself into the checking of balance-sheets for the purpose of determining the exact amount of income which is to be regarded as having been earned in Italy. This control of course necessitates a comparison between the separate accounts of the Italian organisation and the general accounts of the foreign enterprise as well as a comparison with all the data collected by the revenue authorities on their own account.

All these operations, as has already been explained, are part of the method normally employed to determine the taxable income of all enterprises operating in Italy, whatever the nature of their activities.

There is nothing special to add in regard to *banks* or *light and gas companies*.

Insurance companies are required to keep for their Italian portfolio a separate balance-sheet distinct from that of their foreign portfolio. The particulars of the Italian balance-sheet are the basis for determining the income taxable in Italy.

As regards *transport enterprises*, no special remarks are called for by the subsidiaries of foreign companies operating tramways and secondary railways in Italy. These are treated on the same footing as all national enterprises. A special word, however, must be said about the International Sleeping and Restaurant Car Company. This company has no separate balance-sheet for Italy, but submits to the financial administration its general balance-sheet divided into as many parts as there are countries where it operates.

In order to determine the income on which the company is liable in Italy, the Treasury takes as its basis the results of the section in the general balance-sheet referring to Italy ; it checks this section in the light of its information as to the company's total receipts in Italy, both from sleeping-cars and restaurants.

The determination of the company's taxable income in Italy has not as yet been a cause of serious dispute. The Treasury and the representative of the company have nearly always found it possible to come to an agreement.

As regards *telegraphs and telephones*, the former are a Government monopoly. When telephone services are not in the hands of the State, they are granted to private companies under Government control. The question now before us does not therefore arise, for there is, in Italy, no organisation belonging to international telephone or telegraph enterprises.

The question does, however, arise in connection with the company operating telegraphic communications by cable (*Italcable*). This company has some lines with its own cables ; on others its cables are linked to those of foreign companies.

The income from communications along the cables used jointly thus has to be allocated between *Italcable* and the foreign companies, for it is necessary to determine the taxable income of the Italian company. It may be mentioned that this apportionment of income, though presenting many difficulties, is nevertheless facilitated by the terms of the service concession and the clauses of conventions concluded between *Italcable* and foreign companies.

In any case, it must be borne in mind that the law enacts no special methods for taxing *Italcable* and, as a rule, the matter is decided by friendly agreement.

A few words now concerning *mining enterprises*.

In Italy, and particularly in Sardinia, there are numerous organisations for mineral extraction belonging to foreign enterprises. In accordance with the general rule, the taxation of these establishments is based primarily upon the different balance-sheets. In order to check the latter, the revenue authorities have special recourse to information as to the annual quantity of raw materials extracted, the output of mineral substances worked up for export from these raw materials and the cost of these substances.

The income from mineral extraction is fixed by the administration on the basis of this information. The administration does not, however, take account of the income from the treatment of these minerals when they are worked up abroad by the parent company.

B. NATIONAL ENTERPRISES WITH BRANCHES OR SUBSIDIARIES ABROAD.

I. GENERAL METHODS OF ALLOCATION.

As already mentioned, enterprises having their head office in Italy which have no permanent organisation with its own separate accounts abroad have to pay tax on movable wealth in respect

not only of their activities in Italy, but of their foreign activities. The income from the latter is to be regarded as earned in the place where the enterprise has the centre which directs the whole of its economic activity and upon which the results of all its operations converge.

If the enterprise has a foreign branch with accounts separate and distinct from those of the central seat, the law expressly exempts from tax on movable wealth the separate income earned by the branch, which accordingly has to be deducted from the total income taxable against the central seat.

In such cases, the revenue authorities determine the income to be ascribed to the branch by taking as a basis the separate accounts of the branch and comparing them with the accounts of the central seat. The purpose of this comparison is to rectify any transfer of gains or losses from one establishment to the other. Other aids to checking are a knowledge of the amount for which the foreign branch is assessed by the country where it operates, and comparison with the amount for which branches of a foreign enterprise engaged in the same line of industry or commerce are assessed by the Italian Government.

II. ALLOCATION OF PROFIT TO REAL CENTRE OF MANAGEMENT WITHIN THE COUNTRY.

If an enterprise has only its real centre of management in Italy, while all its productive operations are transacted abroad, there is no jurisprudence allowing a portion of the income from these operations to be ascribed to the central seat.

The Law of August 12th, 1927, exempts from tax on movable wealth the income earned abroad by branches, provided that these branches have their own separate accounts.

Prior to this law, jurisprudence was definitely in favour of declaring the whole of the foreign income taxable against the real centre of management. This decision was based upon the view that the place from which an enterprise is managed and administered is the place where the whole activities of the enterprise are centred; this is the place, therefore, where the income must be considered to have been produced. Undoubtedly, management and administration are not merely among the factors of production, but necessary prerequisites, *sine qua non* conditions of the material activities of manufacture and sale. It is the management which organises, initiates and feeds the enterprise's whole work, with the result that, if the management fails, the whole life of the business is suspended.

Since the publication of the Law of August 12th, 1927, the income of an enterprise which does business abroad without having a foreign branch with separate accounts is taxable in its entirety against the central seat, in virtue of the jurisprudence explained above.

It is different when the enterprise does business abroad through branches having their own accounts, the central seat merely keeping a record of expenses.

Can part of the income of the central seat be taxed as representing income earned abroad by branches? Can the exemption granted to the central seat's income by the Law of August 12th, 1927, be refused to this part of it? No judgments have yet been given which would furnish jurisprudence on these questions. The silence of the courts may be due to the fact that there are in Italy no enterprises which have only the centre of management in the country, a centre entirely detached from all industrial or commercial administration proper. Be that as it may, there is not sufficient evidence to furnish an answer to the question.

C. HOLDING COMPANIES.

I. HOLDING COMPANY CONTROLLING ONE OR MORE FOREIGN SUBSIDIARY COMPANIES.

There are no rules for determining the income of holding companies, which are subject to the general regulations governing the taxation of all other companies.

Consequently, a holding company having its head office in Italy is liable to tax on movable wealth in respect of its own income, subject to the following observations :

(1) A holding company cannot be taxed on its dividends from shares in an Italian company, because, as already pointed out, these dividends have already paid tax as income of the company that distributed them.

On the other hand, a holding company's dividends from shares in a foreign company help to make up its Category B income, which is taxable in Italy against the holding company.

If the company is not purely financial, but is industrial and commercial (as may be the case with trusts) and has an independent subsidiary abroad, the dividends from the shares of the subsidiary usually contribute towards Category B income, on which the parent company is liable. Except for exemptions granted in certain cases in favour of dividends of this kind, this is the principle applied by the financial administration, which gives a generous interpretation of the law exempting the income of branches with separate accounts.

(2) A holding company cannot be taxed directly on interest from bonds issued by *Italian companies*, because, as explained before, this interest is taxable against the company issuing the bonds, subject to the latter's right of refund against the recipient of the interest. The only possible obligation upon the holding company is to refund the tax to the company that issued the bonds ; but that is a question of no concern at all to the financial administration. If, however, the interest is in respect of bonds issued since September 30th, 1926, it is exempt from tax on movable wealth and cannot therefore be taxed against the company that pays it ; thus the holding company is not bound to refund.

Interest on bonds issued in Italy by *foreign companies* is governed as a rule by the regulations applying to the taxation of dividends. Accordingly, it goes to make up Category B income, on which the holding company is liable.

(3) A holding company has to pay tax on movable wealth in respect of all income from speculative dealings in its holdings of securities, whether these are the property of one or more Italian companies, or whether they belong to one or more foreign companies.

II. LOCAL SUBSIDIARY COMPANY CONTROLLED BY A FOREIGN HOLDING COMPANY.

When a foreign holding company controls a national company because it holds its shares, it does not thereby become subject to tax in Italy.

The Italian administration is content to tax the national company in respect of the income it earns and takes no account of the parties to which this income is distributed.

In the case of interest which the national company pays on its own bonds, the administration collects tax from the debtor company without regard for the creditor. The latter, however, may be required to refund the tax to the debtor company, a proceeding with which the administration is not concerned.

Annex.TABLE OF TARIFFS.

I. TAX ON BUILDINGS.		Per cent
Basic tax		10
Additional percentages :		
Collected on behalf of the provinces :		
50 per cent (minimum) and 75 per cent (maximum) of the basic tax.		
Collected on behalf of the communes :		
50 per cent (minimum) and 125 per cent (maximum) of the basic tax.		
II. LAND TAX.		Per cent
Basic tax		10
Additional percentages :		
Collected on behalf of the provinces :		
50 per cent (minimum) and 100 per cent (maximum) of the basic tax.		
Collected on behalf of the communes :		
200 per cent (minimum) and 500 per cent (maximum) of the basic tax.		
III. TAX ON INCOME FROM PERSONAL PROPERTY.		Per cent
	Class of Income	
A. Incomes derived exclusively from capital (interests, dividends, rents, etc.)		20
B. Income resulting from the co-operation of capital and labour (industrial and commercial incomes, etc.) :		
Normal tax		14
Rate applicable to agricultural profits accruing to farmers		7
C. (1) Income from labour of an uncertain and variable nature and derived from the carrying on of an independent profession		12
C. (2) Income from labour consisting of fixed and determined amounts, such as salaries, wages, bonuses, etc., paid by private employers or generally by enterprises which are not of public utility or of public interest and income not derived from capital or labour, such as life annuities and similar incomes		9
D. Salaries, wages, pensions and compensation paid by the State, provinces and municipalities, welfare institutions and by various enterprises of public utility or common interest, etc. ;		
Salaries and emoluments of public officials and of employees		8
Workmen's wages		4

IV. TAX ON AGRICULTURAL INCOME REGARDED AS PERSONAL PROPERTY.

	Per cent
Income and profits derived by the landlord cultivating his own land directly or renting it to a <i>métayer</i> or <i>colon partiaire</i> ¹	5
Profits of the <i>colon</i> or <i>métayer</i> ¹	2.5

V. COMPLEMENTARY TAX.

(Abridged Tariff.)

Amount of income (In lire)	Percentage rate of tax
3,000	1.00
5,000	1.22
10,000	1.61
20,000	2.12
50,000	3.05
100,000	4.01
200,000	5.28
500,000	7.60
1,000,000	10.00

The rate of tax applicable to any intermediate income between those shown in the present table may be obtained by raising the income in question to the 0.39637th power and by multiplying it by the fixed proportional coefficient 0.048186 — *i.e.*, if R is the rate required and I is the income, the formula will be as follows :

$$R = 0.048186 I^{0.39637}$$

Before the percentage is applied, it is eventually necessary to round off the taxable income in the following manner :

Income Between and	To the nearest multiple
3,000 5,000	50
5,000 10,000	100
10,000 20,000	200
20,000 50,000	500
50,000 100,000	1,000
100,000 200,000	2,000
200,000 500,000	5,000
500,000 1,000,000	10,000

¹ A *métayer* or *colon partiaire* is a tenant who, unlike the *fermier* (farmer), does not pay a fixed rent in cash, but pays a rent which varies according to the yield of the land and which is usually in kind or partly in cash and partly in kind.

LATVIA

BY

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PART I. — GENERAL DESCRIPTION OF DIRECT-TAX SYSTEM¹

In Latvia, the periodical taxes on income are as follows :²

- Graduated income-tax ;
- Tax on income from capital ;
- Tax on urban properties ;
- Tax on rural properties ;
- Taxes on trade and industry.

The income-tax is a graduated tax to which companies are subject as well as individuals ; it is imposed afresh upon income already liable to one of the other taxes and is also levied upon all income that does not come within the scope of any of those taxes.

The tax on income from capital is levied upon the income from securities issued by the State, by public corporations and by enterprises whose head office is in Latvia, and upon the income from all capital invested in the country in the form of deposits, loans, securities, etc. The tax is proportional and is collected at the source.

Similar to this tax is the special tax on advances made by credit establishments on security ; this tax, however, is borne, not by the creditor, but by the debtor.

Taxes on urban and rural properties are land taxes imposed, in the one case, upon real estate in towns, in the other, upon country estate. Both are proportional taxes and only affect income derived from land and buildings in Latvia.

The taxes on trade and industry are divided into the *patente* tax, the profits tax, and the capital tax.

Patente tax is based on turnover, and industrial and commercial enterprises are divided into a number of categories, each with its own rate of tax. In the case, however, of credit and insurance establishments, the tax is based, not on turnover, but on the registered capital.

The profits tax, as its name implies, is assessed on the net profits of an enterprise, and the capital tax, which is peculiar to companies, is computed by applying to the capital of the taxable enterprise a certain rate varying with the profit.³

I. TAXPAYERS.

(a) INDIVIDUALS.

An individual's fiscal domicile is the place where he permanently resides.

Liability to tax in Latvia depends not so much upon a taxpayer's domicile as upon the source of his income. We shall see under the heading "Taxable Income" the exceptions to and qualifications of this rule. The taxes to which individuals, like all other taxpayers, are liable are

¹ Legislation in force on March 1st, 1933.

² Compilation of Laws 61, *Official Gazette* No. 90, 1920, *Collection of Laws* 142, 1928, *Official Gazette* No. 131, 1928 and *Collection of Laws* 43, 1929, *Official Gazette* No. 65, 1929.

³ The following figures show the percentage contribution of each of these taxes to the total State budget : income-tax, 2.25 ; urban estate tax, 1.07 ; rural estate tax, 0.51 ; *patente* tax, 0.39 ; tax on commercial and industrial profits, 2.20 ; total, 6.42.

the graduated income-tax, the taxes on urban and rural properties, tax on trade and industry and the tax on income from capital.

If a person not domiciled in Latvia resides there for more than six months in the tax year and is not in receipt of income taxable in Latvia by reason of its source, such person will none the less be liable to pay tax on a certain income figure, computed for the whole year on the basis of certain external evidence and his standard of living. When a person spends less than six months in Latvia, his taxable income is determined, not empirically, but from the income he has actually received during his stay in the country.

(b) PARTNERSHIPS.

Partnerships, which include general partnerships, joint ventures, *de facto* associations and other associations not possessing legal entity, are liable to the same taxes and taxed under the same conditions as individuals. They do not, however, in themselves constitute taxable entities and, while the taxes are computed on the basis of the income they enjoy, the tax is assessed against each member or partner and is divided between them according to their respective shares in the partnership or association ; if the amount of individual shares is not known, the tax is divided *per capita*.

(c) COMPANIES.

Companies comprise all associations with a legal entity — *i.e.*, share companies, limited partnerships with share capital and co-operative societies. These companies are domiciled where they have their real centre of management, in most cases, that is, at their registered office. They are liable under the same conditions as individuals and partnerships (constituting, of course, entities taxable as such), but, for purposes of taxes on trade and industry, they have always to produce their balance-sheet and are taxed on the basis not only of their turnover and profits, but of their registered capital.

2. TAXABLE INCOME.

Income liable to taxation is divisible into income from real estate, income from capital, industrial and commercial profits, salaries and wages, remuneration of the liberal and kindred professions, and miscellaneous income.

Let us now consider the taxes on each of these classes of income, having regard to the origin of the income and the domicile of the recipient.

Income from Real Estate. — This income is in the first place liable, according to its nature, either to the tax on urban properties or to the tax on rural properties. These two taxes are strictly territorial and the domicile of the person who enjoys landed income is of small importance, the necessary and sufficient condition of liability being that the taxable income is derived from real property in Latvia. Income from urban estate is further liable to income-tax, but not the income from rural estate. Landed income from abroad is never liable to income-tax, even if the recipient lives in Latvia.

Landed income includes only income from the property or from a property right to the soil, and the law exempts from income-tax agricultural income and income from similar activities (stock-breeding, market-gardening, fruit-growing, forestry, fisheries, etc.), which also do not come within the scope of the tax on income from rural property.

Income from Capital. — By capital yield is meant all income from shares, bonds and other securities, from deposits, current accounts, loans, etc., to the exclusion of capital which a man invests in his own business or enterprise.

If the income is from securities or interest paid in any form whatever by public enterprises or credit establishments, the tax on income from capital is deducted at the source (subject to various exemptions we shall deal with under the heading of assessment), whatever the domicile or residence of the recipient.

Further, such income, whatever its source, will be liable to income-tax if it accrues to persons domiciled in Latvia. Thus, as regards the first of these taxes, fiscal liability is based upon the source of the income and, as regards the second (in so far as it is imposed on the income now in question), on the recipient's domicile.

Industrial and Commercial Profits. — This income, which further includes all receipts of whatever origin associated directly or indirectly with the exercise of a business or industry, is liable to the various taxes on trade and industry, which we shall discuss in detail under the heading "Assessment" (pages 289 and 290), and is also liable to income-tax. Both taxes are payable only if the enterprise has its head office or an establishment in Latvia.

The income from participations in such enterprises is taxable under the same conditions as the profits of the enterprises themselves.

Salaries and Wages. — Salaries and wages, which include all kinds of remuneration and advantages arising out of services performed on behalf and under the authority of another person, are liable only to income-tax.

In order that this tax may be due, the taxable remuneration must represent services accomplished in Latvia, or the remuneration must be paid in Latvia.

Income from the Liberal and Kindred Professions. — This heading embraces the remuneration of doctors, lawyers, teachers and persons engaged in artistic, scientific or literary work.

Here, too, only income-tax is collected and it is only due if the person exercises his calling in Latvia.

Miscellaneous Income. — Under this heading are included retiring pensions, various allowances, life annuities paid by insurance companies, authors' copyrights and patent royalties devolving upon heirs, and other income not included under any of the above headings.

Such income is only taxed in Latvia if it accrues to persons domiciled there (this income is liable to no other tax than income-tax), except as regards pensions paid by public banks in Latvia.

Extraordinary income, like single gifts, bequests, dowries, insurance payments and the surplus value of property, also soldiers' pay on active service, is not taxable. Nor does taxable income include family allowances paid by the State and public corporations to their officials, or insurance benefits paid by the State or insurance funds in case of sickness or accident.

3. ASSESSMENT OF TAX.

General Remarks : Returns, Procedure, Appeals.

The only taxes for which the taxpayer need not furnish a return are the tax on income from capital and the tax on income from rural estate. For all others, a return must be furnished annually (on a date which will be mentioned in dealing with the assessment of each tax), except for tax on income from urban estate, for which returns are triennial.

These returns are sent to the tax inspectors, who have wide powers to obtain from public administrations and enterprises and from the taxpayer all information necessary for checking the returns.

The tax is assessed by "tax committees", presided over by inspectors of the Administration, who are aided by assessors chosen from among taxpayers. *A fortiori* these committees have the same rights of control and enquiry as tax inspectors.

Taxpayers may contest the decisions of committees, first by appealing to the committee and then by appeal to the "Central Tax Committee" at Riga, which is made up of officials of the different administrations and representatives of taxpayers. A final appeal lies with the Senate — that is, the first chamber of the legislative body.

These appeals must be lodged within certain time-limits fixed for each case and varying, as a rule, from a fortnight to one month from the date of serving the assessment notice.

Further, failure to make a return or to observe the provisions of the law and the orders of committees and refusal to comply with the requests of committees or inspectors for information render the offender liable to a fine and may deprive him of his rights of appeal.

Tax on Income from Urban Estate.

Determination of Taxable Income. — The taxable income is obtained by deducting from gross income the cost of maintaining and working the estate. These costs are reckoned according to the nature of the property and the purposes for which it is used. The amount is fixed by the Finance Minister and varies from one town to another between 20 and 95 per cent of gross income, according to the property.

Exemptions. — The following property is exempt from this tax : estates belonging to the Government and to public corporations or to religious and cultural foundations, charitable and educational institutions, hospitals, etc. ; also, subject to reciprocity, premises belonging to foreign diplomatic representatives. Moreover, no tax is collected if it amounts to less than 2 lats per estate. New dwelling-houses are not taxable for the first three years.

Computation of Tax. — The rate is 1½ per cent of the rental value of the property ; 75 per cent of the yield goes to the commune in which the property is situated.

Tax on Rural Estate.

Determination of Taxable Income. — The rental value on which tax is levied and which must correspond to the theoretical net income of the estate is determined by the Administration on the basis of the land register and all other relevant data.

Exemptions. — The exemptions are in principle the same as for the tax on urban estate. But property the rental value of which does not exceed 500 lats is tax-free, and new property, brought into existence under agrarian reform, is exempt from tax for the first six years.

Computation of Tax. — The rate is 1½ per cent, of which one-third goes to the local commune.

Tax on Income from Capital.

Determination of Taxable Income. — This tax is imposed on :

- (1) Income from securities (bonds, shares, founder's shares, etc.) issued by the State, public corporations and enterprises, private companies and enterprises ;
- (2) Interest on deposits and current accounts with public banks, private banks, etc., and on loans and advances to these establishments.

It should be noted that this tax is levied exclusively upon the incomes enumerated and that interest on loans between private persons and income from foreign securities are not liable.

Since this tax is collected at the source, the recipient of taxable income does not need to make a return to the Treasury.

The rate of the tax is 5 per cent, and, owing to the method of collection, no question of abatement, deduction, etc., can arise.

Credits opened or advances granted by State, municipal or private banks on pledges in the form of securities or bills are liable to a special tax amounting per annum to 0.396 per cent of the sum advanced. The banks pay this tax in the course of the month following the closing of their accounts and may recover from the borrower.

Taxes on Trade and Industry.

As already mentioned, industrial and commercial enterprises are liable to a *patente* tax, fixed on the basis either of turnover or of the enterprise's registered capital (banks and insurance enterprises); further, they are liable to profits tax, computed on the basis of net profits, and to a tax on the registered capital, which concerns only companies.

Determination of Taxable Sum.

Persons liable to the taxes on trade and industry have to file a return with the fiscal administration before April 1st of each year, giving their turnover, profits and any other particulars which may help to assess these taxes. The date is advanced to February 1st for enterprises that have been established in the course of the previous year.

Patente tax being based on turnover, it is not necessary to deal in detail with the methods which are used to ascertain this turnover; the Administration fixes it, of course, by reference to the returns, the accounts of the enterprise, if any, and other evidence derived from various sources which, in the absence of accounts, enable the turnover to be determined by a process of assumption.

Nor does any difficulty arise in connection with insurance enterprises and banks; the *patente* tax due from them is determined by reference to their operations, and this applies also to the tax on the capital of companies.

The position is different in the case of profits tax. The law prescribes that the net profits liable to this tax shall be determined in two ways: empirically, by applying a certain coefficient to turnover, or on the basis of the enterprise's accounts.

Normally, enterprises not belonging to companies are assessed to profits tax on the presumptive method and, if the taxpayer wishes to be taxed on the basis of his accounts, he must make a statement to that effect when submitting his return, while his accounts must be closed before May 1st of the tax year. He must also submit his books to the tax inspector, if requested.

For purposes of assessing taxable profits empirically, commercial and industrial enterprises are divided, respectively, into 223 and 194 kinds. For each kind, there are minimum and maximum profit coefficients, determined with due regard to the special conditions of each kind. The net taxable profit is obtained by applying to the enterprise's turnover the coefficient for that kind of business.

If the application of these coefficients gives results that do not appear to reflect the real position of the enterprise, the assessment authorities may reduce the coefficient if the actual profits are lower than the profits reckoned empirically, or may increase it if the actual profits exceed the empirical figure.

Taxation on the basis of accounts is applied to private enterprises which expressly request this method and which satisfy the legal requirements mentioned above, and also to companies. The latter must provide the Administration with a copy of their balance-sheet during the month in which it is approved by the general meeting of shareholders.

In this case, the net profits are the difference between gross profits and expenditure deductible as having been incurred in earning and maintaining those profits.

Gross profits mean all cash receipts and all advantages in kind which an enterprise realises from its operations (whether these are directly or indirectly connected with its purpose or whether they are regular or occasional) or from property in its possession. The following is a fairly complete list of the expenses and items that may be deducted from gross profits in order to obtain the taxable net profit. Unless the contrary appears from the very nature of the expenses in question, the different components of this list are common to all enterprises, whether they belong to individuals or to companies :

(1) Emoluments and percentages of managers, auditors and directors of companies, up to 7,500 lats per head per annum, and on condition that the total deductions on this score do not exceed a certain sum fixed in relation to the registered capital — viz., 10 per cent of the capital for enterprises whose capital is not more than 200,000 lats ; 20,000 lats plus 5 per cent of the capital over 200,000 lats for companies whose capital is between 200,000 and 500,000 lats ; 35,000 lats plus 3 per cent of the capital over 500,000 lats, for companies with capital exceeding the latter amount ;

(2) Salaries, wages and any other remuneration paid to workmen and employees in the enterprise's service :

(3) The cost of improving the lot of the staff and workmen and their families (in particular, contributions to insurance funds, pensions funds, etc., and, subject to some restrictions, expenditure on philanthropic and charitable objects ;

(4) Commissions, brokerage and other remuneration to third parties ;

(5) Cost of purchasing goods intended for sale or other industrial use ;

(6) Cost of letting, ensuring and maintaining premises, equipment and furniture used in the business (big repairs and expenditure on enlarging or improving the business are not deductible, since they increase the value of the property) ;

(7) Allowances for depreciation of corporeal property used by the enterprise up to the amount regarded as normal in view of the actual life-time and depreciation of the property ;

(8) Interest on debts contracted for the purposes of the enterprise (the owner of a business may not deduct interest on capital which he has himself invested in his enterprise) ;

(9) Losses of any kind incurred during the tax year, and doubtful debts ;

(10) Taxes owing to the State and public corporations, except income-tax and profits tax ;

(11) Appropriations by insurance companies for building up their mathematical reserves ;

(12) Appropriations for redeeming the capital of enterprises holding a concession which reverts after a certain time to the State or other conceding parties ;

(13) Sums set aside by long-term credit associations for the redemption of their bonds.

Computation of Tax.

Patente Tax. — The turnover figure calculated as above serves to divide taxpayers into a number of classes with a special rate of tax for each. For banks and insurance companies, however, *patente* tax is fixed on the basis not of turnover, but of registered capital.

Profits Tax. — This is a graduated tax, rising from 5 per cent for incomes not exceeding 2,000 lats to 15 per cent for incomes above 15,000 lats. The tax is also progressive in the case of companies, but its tariff is graduated on the basis of the yield on the capital of the enterprise and goes from 7.5 % up to 17.25 %.

From the profits tax is deducted the amount of *patente* tax already paid, but, if the amount of profits tax is less than the licence tax, no refund is made. Companies which have to submit a balance-sheet and whose profits are below 3 per cent of their capital pay no profits tax.

Half of both these taxes goes to the commune where the enterprise is situated.

Tax on Company Capital. — This tax is levied at the rate of $\frac{1}{4}$ per cent when no profits tax is payable ; otherwise at $\frac{1}{2}$ per cent.

Income-Tax.

Determination of Taxable Sum. — Income-tax is levied, in the first place, on income already liable to one or other of the taxes previously mentioned and also on income, like salaries, wages and remuneration of the liberal professions, on which no tax has been paid. Income-tax returns must be filed before April 15th by individuals and before May 15th by companies.

The taxable sum is the total net income of all classes, less certain deductions of income derived from no specific source.

The law divides income the total of which is liable to income-tax into income from capital, income from land and buildings, industrial and commercial profits, wages and salaries, remuneration of the liberal professions and miscellaneous income. It has therefore to be determined for each of these classes how the net amount is to be computed, before adding them all together :

(1) Income in the first class — *i.e.*, income from capital of any kind — is computed after deducting from the receipts of this class expenditure economically connected therewith and, in the case of income from interest on bank deposits and accounts, the sum of 1,000 lats ;

(2) The taxable amount of landed income is the total net rent or, in the case of land and buildings not let, the net rental value. This amount may not be the same as that upon which the taxes on rural and urban properties were assessed.

(3) Industrial and commercial profits are assessed in the same way as for profits tax.

(4) The expenditure that may be deducted from salaries and wages is fixed empirically at 40 per cent of the income ; only the remaining 60 per cent is taxable.

(5) Remuneration of independent professions includes all the sums in cash (fees, copyrights, etc.) and advantages in kind accruing to those engaged in the liberal professions, art and science. Net income is obtained by deducting from total receipts and advantages in kind all expenses economically connected with this income.

(6) Miscellaneous income includes all income which by its nature cannot be classed under one of the above headings. It includes, in particular, retiring pensions, pensions for disablement, life annuities, income accruing to heirs from patents and copyrights, etc.

This income too is assessed at its net amount. Pensions paid to persons disabled in the war and to the widows and orphans of fallen soldiers are tax-free.

All this net income is added together, including, in the case of a taxpayer with wife or children not of age living under his roof, the income of the latter, except income from their work. The authorised allowances are then deducted, giving the final sum taxable.

The deductions allowed from total net income are :

(1) All expenses incurred in earning and maintaining the income and not already deducted therefrom ;

(2) Interest, annuities and periodical payments due by law to third parties, not relating to any specific source of income ;

- (3) Life-insurance premiums up to 150 lats per annum and sums paid to members of an insurance fund, pension fund, etc. ;
- (4) The various direct taxes, except income-tax, payable by the taxpayer ;
- (5) Family allowances — viz., 240 lats for each person who is regarded by law as dependent upon the taxpayer and whose own income does not exceed 500 lats per annum ;
- (6) In the case of legal entities, a sum equal to 3 per cent of the registered capital or contributions of partners or members.

The following may *not* be deducted from total net income :

- (1) The personal expenditure of the taxpayer and his family ;
- (2) Gifts and presents ;
- (3) Expenditure on improving and enlarging the property and enterprises of the taxpayer ;
- (4) Losses on his property and capital ;
- (5) Expenditure corresponding to non-taxable income (*e.g.*, certain income of foreign origin).

The net amounts having been added together and the above deductions made, the result is the net taxable sum.

Computation of Tax. — The tax is only levied if the taxable sum exceeds 2,000 lats. Its scale is graduated (see Annex) and rises from 58.30 lats for incomes between 2,000 and 2,010 lats to 36.692 lats for incomes of 150,000 lats, plus one-quarter of the income in excess of 150,000 lats.

The method of computation is different for legal entities which pay profits tax (whose profits, that is, exceed 3 per cent of their registered capital). In their case, the income-tax is equal to half the profits tax for the same year.

The income-tax of legal entities which pay no profits tax is computed according to the ordinary rules.

4. COLLECTION OF TAX.

Taxes *payable directly* have to be paid in equal instalments on the following dates :

- Income-tax : on December 31st of the tax year and on March 31st and June 30th following ;
- Tax on industrial and commercial enterprises : on September 30th, November 30th and February 28th ;
- Taxes on urban and rural estate : July 30th and November 30th.

Tax on income from capital, which, it will be remembered, is collected by *deduction at source*, must be paid to the Treasury by the debtor, who deducts it at source.

Income from bonds and other securities : during the month following the payment of interest ;

Interest on sums deposited or on current accounts with public enterprises or banks : during the month in which the accounts are closed.

If the taxable income for the year during which the tax has been paid has substantially diminished, a total or partial remission of tax may be allowed. These remissions and alleviations are governed by rules specially provided for each tax.

PART II. — TAXATION OF FOREIGN AND NATIONAL ENTERPRISES

A. FOREIGN ENTERPRISES.

I. DEFINITION AND GENERAL PRINCIPLES.

The law does not specify what is to be understood by national enterprises. For purposes of the present study, the term includes all enterprises whose real centre of management is abroad. These enterprises are, in principle, liable to tax in respect only of income they derive from Latvia (see Part I, "Taxable Income").

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) *Dividends.*

Dividends of Latvian companies paid to foreign enterprises are subject to the ordinary law and pay the tax on income from capital, which is deducted at the source at the rate of 5 per cent.

A foreign enterprise will also be liable to income-tax on these dividends, if they are among the receipts of an industrial or commercial establishment which the enterprise maintains in Latvia. Again, if such establishment has foreign shares in its portfolio, the dividends therefrom will be liable to income-tax as receipts of the establishment in question.

(b) *Interest.*

What was said above about dividends applies also to *interest* on Latvian *bonds* which the enterprise holds without having an establishment in the country, and to bond interest of any origin if the bonds belong to the portfolio of an establishment in Latvia.

Interest on Unsecured Loans. — As already mentioned, capital-yield tax is imposed, not only on income from Latvian securities, but on interest from deposits, current accounts, etc., with public enterprises or banks in Latvia.

Accordingly, any interest paid to a foreign enterprise under this head will always be liable to tax on income from capital, whether the enterprise has an establishment in the country or not.

Interest derived from Latvia is only taxable if it is among the receipts of an establishment situated in the country. In this case, it will be liable to income-tax, like all other interest accruing to such establishment, including interest on which the tax on income from capital has already been paid.

Interest on Secured Loans. — The fact that a loan is guaranteed by a security situated in Latvia is of no importance from the fiscal point of view, so that what was said with reference to unsecured loans applies here too.

(c) *Directors' Percentages.*

Directors' percentages are liable to income-tax, even if paid to directors whose domicile or head office is abroad.

(d) *Royalties for Use of Patents, Copyrights, Trade-marks, Secret Processes and Formulæ and Similar Income.*

If the holder of a patent or similar rights is not domiciled in Latvia and has no establishment there, no tax is levied upon the royalties he draws from the mere concession of these rights or patents.

But, if these royalties are among the receipts of an establishment in Latvia, they will be liable to income-tax and the taxes on trade and industry in the same way as the establishment's other industrial and commercial receipts.

The same applies if the patent has not been merely licensed, but if its cession is to be regarded as a contribution towards the capital of an enterprise having its head office or an establishment in Latvia. In this case, the patent-holder will be liable, like any other partner or person entitled to a share in the profits of the enterprise, on his share of the taxes due from the concessionary enterprise.

(e) *Rents from Real Estate, Mining Royalties and Similar Income.*

Property situated in towns and in the country is, as explained, liable, respectively, to the tax on urban estate and the tax on rural estate, which taxes are levied upon income from real estate. Income from urban property is further liable to income-tax, but not the income from rural estate. Nor is income from agricultural and similar exploitation liable to income-tax.

All other income from exploitation of the soil is subject to income-tax and to the different taxes on trade and industry.

(f) *Gain derived from the Purchase and Sale of Real Estate, Securities and Personal Property.*

In Latvia, there is a tax on exceptional profits or on increased value. This tax is imposed, in particular, when property is sold at a profit, whether the transaction is an occasional or a regular one.

Income-tax will only be levied if these transactions in real or personal property, corporeal or incorporeal, are directly or indirectly included among the receipts of a business or industry carried on in Latvia.

If these receipts are not connected with a business or industry, they are not liable to income-tax, even if the operation was in the nature of speculation.

(g) *Salaries, Wages, Commissions and Other Remuneration for Services.*

Remuneration in these forms is only taxable if it represents work done in Latvia or if it is paid in Latvia. In either event, taxation is independent of the taxpayer's domicile. The same is true of the various emoluments of company directors.

(h) *Income from a Trust.*

* The question of taxing trusts does not arise in Latvia, the law not recognising these institutions.

(i) *Income from carrying on a Business or Industry.*

If a foreign enterprise is to be taxable in Latvia on its industrial and commercial income, it must regularly carry out profit-making operations, either directly or through its employees thus :

(1) An enterprise which merely buys or sells in Latvia, through a *commission agent or broker*, is not liable in respect of these operations ;

(2) Nor is it liable if it sells its goods to a *local dealer or distributor*, who works on his own account and at his own risk and peril ;

(3) Again, a foreign enterprise will not be liable if it merely uses the services of a *travelling salesman*, whether the latter has power to conclude a contract or not ;

(4) But if the foreign enterprise has an *agent* in Latvia whose business it is to sell to customers out of stock entrusted to him, it will be held liable to tax in respect of this depot ;

(5) The law does not define a *permanent establishment*, but there is no doubt that a foreign enterprise which has more or less permanent installations will be liable to pay tax in Latvia on the operations centred in these installations or establishments.

B. NATIONAL ENTERPRISES.

The law does not define the term "national enterprise" any more than it defines a "foreign enterprise", and we must understand by the term "national enterprise" any enterprise whose seat of management is in Latvia.

As mentioned in Part I, taxation in Latvia is based not so much upon the domicile of recipients of income as upon the source of that income.

The observations in Part I, under the heading of "Taxable Income", make it unnecessary to dwell upon the fiscal treatment applying to each kind of income that these enterprises may derive from abroad.

PART III. — METHODS OF ALLOCATING TAXABLE INCOME

A. FOREIGN ENTERPRISES WITH LOCAL BRANCHES OR SUBSIDIARIES.

I. GENERAL QUESTIONS AND METHODS OF APPORTIONMENT.

(a) BOOK-KEEPING AND ACCOUNTING REQUIREMENTS.

Latvian fiscal law has no provisions as to how the books and accounts of taxable enterprises shall be kept. When, therefore, enterprises are being taxed on the basis of their accounts, the regularity of their books and documents is to be tested according to the rules of the Commercial Code and those of ordinary commercial practice.

Only companies need be assessed on the basis of their balance-sheet and accounts. Other enterprises are assessed on this basis only at their request ; otherwise their profits will be determined by means of coefficients — that is, empirically (see page 289).

(b) METHODS OF ALLOCATION.

The only methods of apportionment provided by the law and actually employed in Latvia are the method of separate accounting and the empirical method. Fractional apportionment is never used. We shall see below the circumstances in which one of the two methods employed is preferred to the other.

I. *Method of Separate Accounting.*

Whatever method may be used to assess the profits that a foreign enterprise earns from its Latvian business, the basic rule is that tax must be assessed exclusively upon the profits that represent business done by branches and establishments situated in Latvia.

The method of separate accounting, however, is only compulsory in the case of enterprises belonging to companies, which, as we know, have to forward a copy of their balance-sheet when making their return. Other enterprises may choose between this method and the empirical method, which consists of applying a coefficient to turnover.

When a foreign enterprise is taxed on the basis of its separate accounts, it forwards along with its return a copy of the special balance-sheet and a copy of the balance-sheet of all operations of its Latvian establishments ; it must also send the minutes of its general meeting, within a month thereof. These last two documents are required to check the special balance-sheet.

The data of this sheet will be compared with the separate accounts of the Latvian establishments and with the documents on which these accounts are drawn up. The usual rules for auditing accounts are observed, but special attention is paid to documents referring to business done with the foreign part of the enterprise, to make sure that the invoiced prices are normal and that no profits have been secretly transferred.

Care is taken to see not only that the various transactions were conducted under normal conditions, but that the net profits are those which would have been ascertained by the application to turnover of the coefficients resulting from the general scale fixed by the tax committees for the different kinds of enterprise.

However, if the net profits, though lower than those resulting from this latter method of calculation, correspond to *bona-fide* accounts and reflect the real results of the Latvian establishment, regarded as a separate enterprise, they are accepted as the basis of taxation.

2. *Empirical Method.*

Taxable profits are assessed empirically in the following cases :

(1) Enterprises not belonging to companies and which have not asked to be based on the results of their accounts ;

(2) Enterprises belonging to companies (the latter are in principle taxed according to their balance-sheet) when their accounts are found inadequate or incorrect.

The empirical figure is reached by applying a certain coefficient to the enterprise's turnover and corresponds to the net profit. Accordingly, when the taxable sum is determined empirically, no account is taken of the expenses deductible when the enterprise is assessed according to its accounts (see page 290).

The coefficient is fixed by the general tax committee on a scale which divides industrial enterprises into classes according to their kind and purpose (see page 289). Minimum and maximum profit percentages are fixed for each class and the tax committee selects the rate it thinks suited to the particular enterprise.

These rates, however, may be reduced to nothing if the taxpayer can satisfy the committee that his real profit is less than the figure resulting from the coefficient. The committee, too, may increase the percentage indefinitely if the latter does not seem to it to reflect the real results of the enterprise.

The turnover figure on which the calculation is based is determined from the accounts or is based on some assumed figure.

(c) APPORTIONMENT BETWEEN BRANCH AND PARENT ENTERPRISE.

1. *Apportionment of Gross Profit of Local Branch to Real Centre of Management abroad.*

The principle of Latvian law that the establishment or branch of a foreign enterprise in Latvia shall be taxed as if it were an independent concern means that all the profits of these establishments are taxable, but they alone.

Hence, no part of the profits of the establishment can be ascribed to the enterprise abroad ; but, if part of the establishment's profit is due to the activities and services of the parent enterprise, that share may be deducted from the taxable profit. It is on this ground that deduction is allowed of commissions, royalties and interest paid to the parent enterprise, provided that these payments correspond to what would normally have been paid to third parties and that the parent enterprise, when invoicing goods supplied to its Latvian branch, includes in the invoice the profits which would normally have been earned, had these goods been sold to third parties.

2. *Apportionment of Expenses of Real Centre of Management to Branch.*

Interest Charges. — If the parent enterprise is to ascribe to its Latvian branch a part of its interest charges and if that interest is to be deductible from the profits taxable in Latvia, the debt

must have been incurred in the interest of the branch or the yield of the loan made over to it. Such interest may be charged to the Latvian establishment in proportion to the benefit the establishment has derived from the borrowed capital.

General Overhead. — The above rule applies *mutatis mutandis* to general overhead. These expenses may be deducted from the Latvian profit if they were incurred on behalf of the establishment or if they were of benefit to it.

3. *Apportionment of Net Profit of Branch to Deficitary Parent or of Parent to Deficitary Branch.*

Given the general principle for allocating gross profits, it follows that the results of the parent enterprise do not affect the sum taxable in Latvia, either when the parent is working at a loss and the Latvian establishment at a profit, or when the position is reversed. In the latter case, the accounts of the taxable establishment will, of course, be examined especially closely.

(d) APPORTIONMENT BETWEEN PARENT ENTERPRISE AND SUBSIDIARIES.

Subsidiary companies have a legal existence apart from the companies which created them. Accordingly, subsidiaries organised in Latvia by foreign companies are taxable like any other Latvian company.

If it appears, however, that these subsidiaries are transferring their profits to the foreign enterprise on which they depend, their accounts may be corrected and, if essential to a fair assessment, their profits may even be computed empirically. This indeed is only in accordance with ordinary law.

II. APPLICATION OF THE METHODS OF ALLOCATION IN SPECIFIC CASES.

(a) INDUSTRIAL AND COMMERCIAL ENTERPRISES.

I. *Selling Establishments.*

As regards selling establishments of foreign enterprises in Latvia, there is no distinction between those which sell in the national market and those which sell abroad.

In order that sales profits may be taxable in Latvia, it is only necessary that the sale shall have been effected by an enterprise established there. The taxable profit will be the profit on which a Latvian enterprise working under the same conditions would itself be liable.

Consequently, a foreign enterprise may invoice its goods at the price at which it would sell them to third parties and, if allocation by separate accounting is employed, the accounts of the taxable establishment will be examined in the light of this principle.

If profits are calculated empirically as a percentage of turnover (see pages 296 and 297, concerning the choice of methods), use will be made of the coefficients applying to commercial enterprises selling the same goods.

2 and 3. *Manufacturing and Processing Establishments.*

The profits and advantages derived from the industrial operations of factories, workshops, yards, etc., owned by a foreign enterprise in Latvia are taxable in the same way as profits from commercial business transacted in Latvia, and the rule governing the examination of the accounts of these establishments will be that their profits must correspond to those which a Latvian industrialist would have earned by similar operations.

If the industrial establishment has a commercial establishment attached to it which sells the manufactured goods direct, the whole profit from production, manufacture and sale is taxable.

The empirical method is also applied in this case and, as usual, obeys the general rules already given.

4. *Buying Establishments.*

The mere fact that an enterprise has an establishment in Latvia whose sole business is to buy goods and sell them to the parent enterprise does not render the latter liable to tax. The establishment must not, of course, carry out any industrial operations upon the goods bought and must not sell to third parties ; otherwise, the dealings come under the cases already dealt with.

5. *Research and Statistical Establishments, Display Rooms, etc.*

These and other establishments not engaging in any industrial or commercial operation and participating only indirectly in the profit-making activities of the enterprise are not taxable.

(b) OTHER KINDS OF ENTERPRISE.

There are no special rules for assessing the profits of insurance companies, transport enterprises, gas, light and power enterprises, telegraph and telephone companies, or mining enterprises, and what was said before concerning allocation methods and the apportionment of profits between branch and parent enterprise applies to foreign enterprises of these various kinds which have establishments or installations in Latvia.

Although not concerned with the allocation of profits, it may be noted that the method of calculating *patenī* tax in the case of banks and insurance companies is not the same as that in force for other enterprises (see page 290).

B. NATIONAL ENTERPRISES WITH BRANCHES OR SUBSIDIARIES ABROAD.

It will be remembered that Latvian enterprises with establishments or branches abroad are not liable in respect of the profits earned by the latter.

In determining the share of foreign establishments in the general results of the enterprise, the principle followed is the same as that applying to foreign enterprises when taxed by the method of separate accounting.

When the empirical method is used, the coefficient is applied not to the total turnover, but only to the turnover of the head office and establishments situated in Latvia.

The position is different if the national enterprise has not a branch, but a subsidiary abroad. The profits paid to it by the subsidiary are dividends — *i.e.*, capital yield ; and this income is liable to tax if it accrues to taxpayers whose fiscal domicile is in Latvia.

C. HOLDING COMPANIES.

There are no special rules for holding companies.

Consequently, a foreign holding company which holds shares in a Latvian company will be liable on the same heads and under the same conditions as any other foreign shareholder or bondholder (for taxation of dividends and interest on bonds paid by Latvian companies to foreign enterprises, see page 293). If, on the contrary, a Latvian holding company holds shares or bonds issued by a foreign company, the income from these securities will be taxable under the same conditions and heads as any other income from capital accruing to a taxpayer domiciled in Latvia from capital invested abroad.

Annex.

TABLE OF TARIFFS.

I. PROGRESSIVE INCOME-TAX.

*Abridged Tariff.*¹

Amount of income (In lats)	Amount of tax (In lats)	Approximate percentage ² of tax in relation to income
2,000	58.30	3
3,000	135.80	4.5
4,000	219.60	5.5
5,000	309.70	6
10,000	854	8.5
15,000	1,506	10
20,000	2,206	11
25,000	2,958	12
30,000	3,758	12.5
35,000	4,610	13
40,000	5,510	13.5
45,000	6,462	14.5
50,000	7,462	15
60,000	9,614	16
70,000	11,966	17
80,000	14,518	18
90,000	17,270	19
100,000	20,222	20
110,000	23,324	21
120,000	26,524	22
130,000	29,826	23
140,000	33,226	24
150,000	36,692	24.5

II. TAX ON INCOME FROM CAPITAL.

Tax on income from capital proper : 5 per cent of the income.

Tax on interest debited on current accounts and overdrafts by public bodies and banking institutions : 0.396 per cent of the interest.

¹ In the complete tariff, which is not reproduced here on account of lack of space, the tax increases in arithmetic progression with an irregularly increasing ratio.

² The percentage is rounded off to the nearest $\frac{1}{2}$ per cent.

III. TAX ON INCOME FROM URBAN REAL ESTATE.

A percentage of $1\frac{1}{2}$ of the rental value.

IV. TAX ON INCOME FROM RURAL REAL ESTATE.

A percentage of $1\frac{1}{2}$ of the cadastral income or, in the absence of a cadastre, of the rental value of the property.

V. TAXES ON BUSINESS AND INDUSTRY.

A. Patente Tax.

1. Commercial Enterprises.

Category of the taxpayer	Amount of tax (In lats)
1st category (turnover in excess of 200,000 lats)	300
2nd category (turnover between 100,000 and 200,000 lats)	150
3rd category (turnover between 50,000 and 100,000 lats)	75
4th category (turnover between 10,000 and 50,000 lats)	30
5th category (turnover not exceeding 10,000 lats)	5

2. Industrial Enterprises.

Category of the taxpayer	Amount of tax (In lats)
1st category (turnover in excess of 500,000 lats)	600
2nd category (turnover between 200,000 and 500,000 lats)	300
3rd category (turnover between 100,000 and 200,000 lats)	150
4th category (turnover between 50,000 and 100,000 lats)	75
5th category (turnover between 10,000 and 50,000 lats)	30
6th category (turnover between 5,000 and 10,000 lats)	5

3. Banking Insurance Institutions.

Category of the taxpayer	Amount of tax (In lats)
1st category (statutory capital in excess of 1,000,000 lats)	600
2nd category (statutory capital between 500,000 and 1,000,000 lats)	300
3rd category (statutory capital between 200,000 and 500,000 lats)	150
4th category (statutory capital between 50,000 and 200,000 lats)	75
5th category (statutory capital between 10,000 and 50,000 lats)	30
6th category (statutory capital not exceeding 10,000 lats)	5

B. Tax on Profits.

Amount of profit (In lats)	Tax applicable to the fraction of profits included between the two figures of the 1st column (Percentage) ¹	Amount of tax corresponding to the 2nd figure of the 1st column (In lats) ¹
Up to 2,000	5	—
Between 2,000 and 5,000	7	350
Between 5,000 and 8,000	9	720
Between 8,000 and 11,000	11	1,215
Between 11,000 and 15,000	13	1,950
Over 15,000	15	—

¹ Of which half is collected on behalf of the communes.

Special Provisions applicable to Enterprises subject to the Rules of Public Accountancy.

If the *yield is less than 3 per cent* of the statutory capital, the tax on profits is not payable; the only tax which is applicable is the special tax on capital at the rate of $\frac{1}{4}$ per cent.

If the *yield exceeds 3 per cent* of the statutory capital, the tax on profits is calculated according to the table given below and the special tax on capital is assessed at the rate of $\frac{1}{2}$ per cent.

Percentage of the yield in relation to the statutory capital	Percentage of the tax on profits applicable to the total profits
3.01	7.5
4	8.07
5	8.64
6	9.21
7	9.80
8	10.36
9	10.93
10	11.50
11	12.09
12	12.66
13	13.23
14	13.80
15	14.38
16	14.95
17	15.52
18	16.24
19	16.68
20	17.25

If the net profits exceed 20 per cent of the statutory capital, the rate of tax amounts to 17.25 per cent of the total profits plus 0.75 per cent for the fraction of profits in excess of 20 per cent.

LUXEMBURG

BY

The Direction of the Tax Administration.

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PART I. — GENERAL DESCRIPTION OF INCOME-TAX SYSTEM.¹

The object of direct taxation is to distribute public burdens according to the contributive capacity of taxpayers. Luxemburg legislation has adopted, as criteria of this capacity, income on the one hand and property on the other. Taxes on income comprise the income-tax proper, the surtax and the tax on coupons; there is further a complementary tax on property. All these taxes apply alike to individuals, partnerships and companies.

Income-tax proper is imposed, in principle, upon the total net income of each taxpayer, excluding such income as dividends, which will already have been taxed as income in the hands of other taxpayers, and income on which coupon-tax has already been levied.

Income-tax is on a graduated scale and the taxpayer is granted certain basic alleviations and allowances in respect of family dependents. It is further subject to "additional centimes" levied on behalf of the communes, the percentage varying locally.

Surtax is an addition of the income-tax proper² and is imposed upon incomes above a certain figure.

Unlike the income-tax, it is not subject to additional centimes. It was introduced as a separate tax, because, although it was intended to increase the proportion of the fiscal burden borne by large incomes, it was not desired to add to the contribution of these incomes towards the communal budgets.

Coupon-tax is a tax on the interest on bonds issued by the State and by Luxemburg public corporations and companies. It is a proportional tax, but varies with the rate of the interest on which it is levied. Although this tax is classed among income-taxes, it is of a mixed character, for its rate includes the complementary tax on the capital from which the interest is derived.

Complementary tax is levied, at the fixed rate of 0.50 franc per thousand francs of taxable property, on personal and real estate above a certain value. Like income-tax, it is increased by additional centimes on behalf of the communes.

All these taxes,² except coupon-tax, which is deducted at the source, are payable by the taxpayer himself.

The following account will show what exceptions and qualifications must be made in regard to the foregoing definitions which were only introductory remarks.³

¹ Legislation in force on June 1st, 1933.

² The provisions relating to the taxes discussed in the present study are contained in the Law of November 26th, 1927 (Executive Regulations of January 4th, 1928), as amended by the Law of June 19th, 1929.

³ The following figures show the relative importance in the budget of the Grand-Duchy of the different taxes mentioned above. According to the 1931 estimates, direct taxes yield 48 million francs out of a total revenue of 233,350,000 francs. The 48 millions are made up as follows; income-tax, 30 millions; surtax, 11 millions; coupon-tax, 2½ millions; complementary tax, 4½ millions. The communal centimes, levied in addition to the income-tax and complementary tax, are estimated at 59 millions.

I. TAXPAYERS.

(a) INDIVIDUALS.

The personal status of the recipient of income liable to coupon-tax is a question of no importance, as this tax is imposed indiscriminately upon all interest from bonds issued by the State and by Luxembourg public corporations and companies.

As regards income-tax, on the contrary (and therefore surtax), and the complementary tax, both liability and its scope, although independent of the taxpayer's nationality, do nevertheless depend upon residence.

Without attempting to define so indeterminate a notion as that of residence, we may say that jurisprudence opposes *residence* or *fiscal domicile* to the *civil domicile* and merely temporary *abode* (*simple séjour*). Residence implies "a stay of some duration combined with other *de facto* circumstances that establish an intention actually to reside in a certain commune", and a person who has a house in Luxembourg capable of permanently accommodating himself and his family under conditions in keeping with his social status possesses a residence in the Grand-Duchy, even though he may himself travel and work abroad for the greater part of the year.

Taxpayers regularly residing in the country are, in principle, liable in respect of all their income of whatever origin. Their fiscal liability is, as we may call it, unlimited, and the income and property in respect of which they are liable are discussed in detail under the heading "Taxable Income" (see pages 308 and 309).

Individuals who are not regularly resident in the country but live there normally for at least six months in the year (whether consecutively or not) are liable, like regular residents, in respect of all their income, but only in proportion to the length of their stay.

Individuals who reside in the country for less than six months are only liable in respect of income derived from and property situated in the country; they are subject to limited fiscal liability. The extent of their liability is explained under the heading "Taxable Income" (see pages 308 and 309).

(b) PARTNERSHIPS.

The fiscal law of Luxembourg regards as partnerships (*sociétés de personnes*) *de facto* associations, partnerships (*sociétés en nom collectif*) and limited partnerships with or without share capital (*sociétés en commandite simple ou par actions*). These partnerships constitute taxable entities.

The tax on profits and income is levied upon the partnership as such and not upon the partners individually.

Just as the fiscal liability of individuals depends upon their residence, so that of partnerships depends upon the place of their head office (*siège social*). But if that head office is only nominally abroad and the partnership's real centre of management is in Luxembourg, the partnership is treated as if its head office were in the country.

(c) COMPANIES.

This term comprises co-operative societies and share companies.

What was said above as to the importance of the head office and centre of management applies *a fortiori* to companies.

Companies, like partnerships, are in principle subject to the same fiscal treatment as individuals. This, however, does not apply to Luxembourg holding companies, which are exempt from direct taxes (see page 326).

2. TAXABLE INCOME.

A. *Taxes on Income.*

The law regards as taxable ;

(1) Income from personal property — viz. :

(a) Interest on secured and unsecured debts and on loans of any kind ;

(b) Interest on capital invested in a life annuity ;

(c) Interest on bonds issued by the State, foreign Governments, public corporations and by companies and other enterprises of all kinds ;

(d) Interest, dividends and income from shares of all kinds in partnerships or companies of any kind, both national and foreign.

(2) Income and other advantages accruing to a taxpayer in virtue of a right of ownership, usufruct, use or occupation, in respect of any kind of real estate in the Grand-Duchy. (Such income includes, not only income from letting or advantages independent from human labour, but also the income from agricultural property worked by the owner himself with his own capital.)

(3) The profits of trade and industry. These include all the products of the association of capital and labour — viz., the products of any commercial or industrial undertaking or occupation, and of any agricultural, forestry or mining enterprise. (Here, the term " income from agriculture or forestry " means, not the income which the owner earns by putting his property to account, but the income which a farmer or tenant earns by working land belonging to another person.)

(4) The product of man's labour and other periodical income not included under 1 to 3 above. This class comprises the salaries, wages, etc., of all those who work in any capacity on behalf of others (officials, employees, soldiers, workmen, domestic servants, etc.) ; directors' percentages ; the income and remuneration of the liberal professions, literature, art and science ; pensions, life annuities and other advantages which cannot be regarded as income from personal or real property.

Taxpayers subject to an *unlimited fiscal liability* are taxable on all income enumerated above, whatever its origin, except income from real estate situated abroad. Also, dividends and other income enumerated under 1 (d), which have already paid income-tax as profits of a taxable company, are not taxed a second time in the hands of the shareholder or partner. Nevertheless, as we shall see, account is taken of such income in fixing the rate of tax applicable to the total income.

Taxpayers subject to a *limited fiscal liability* — i.e., individuals who are not resident in Luxemburg for six months and companies or partnerships which have neither their head office nor their real centre of management in the country — are only liable in respect of income from :

(1) Commercial or industrial enterprises operated by them in Luxemburg ;

(2) The profession or occupation they follow in Luxemburg or the functions they discharge in Luxemburg companies or commercial or industrial enterprises ;

(3) Capital of all kinds they have invested in such companies or enterprises ;

(4) Real property owned by them in the Grand-Duchy.

Further, as regards income from capital invested by these taxpayers in Luxemburg, the same restrictions must be made as in regard to income of this kind accruing to taxpayers subject to an unlimited fiscal liability.

B. *Complementary Tax on Property.*

Under the law, this tax is imposed upon the following property :

- (1) Real estate in Luxemburg with its appurtenances ; mines, quarries, mining concessions, rights of usufruct, use and occupation of immovable property having an appreciable cash value ;
- (2) Capital invested in trade or industry or in agricultural, forestry and mining enterprises ;
- (3) Movable capital and securities of every kind, debts, foreign shares and bonds, shares in foreign partnerships, banknotes, precious metals, the surrender value of life insurance policies and of annuities, life annuities payable in cash or in kind.

With regard to (1), complementary tax is never levied upon real estate situated abroad, even if the property belongs to persons resident in Luxemburg.

As regards (3), it is not the intention of the law that shares representing capital already taxed against a company shall be taxed again in the hands of the shareholder. This exemption corresponds to the exemption from income-tax of dividends representing profits on which a company has already paid tax. This means that, in practice, only foreign shares and securities are taxable in the hands of their owners.

As with income-taxes, persons resident in the Grand-Duchy have an unlimited fiscal liability and are therefore liable on all the property enumerated above, with the two restrictions just mentioned.

Taxpayers whose liability is limited need only pay the tax on property situated in Luxemburg — *i.e.*, real estate within the country (see (1)), capital invested in an industrial, commercial, agricultural, forestry or mining enterprise in Luxemburg and debts, the debtor of which resides in the Grand-Duchy.

3. ASSESSMENT OF TAX.

A. INCOME TAXES.

(a) *Computation of Taxable Income and Abatements.*

Income from Capital. — This income is taxable on the basis of its amount during the year preceding the tax-year. It is taxed up to its full amount without any abatements at all. An exception, however, is made in the case of income from capital derived from abroad which has already been taxed abroad at the source, if this fact has been declared in the recipient's return.

If the amount of income is unknown, it is estimated at 5 per cent per annum of the capital to which it refers.

Assets employed in a trade or business are not held to yield income apart from the profits of all kinds which may result from such activities.

Income from Land and Buildings. — In the case of buildings — *i.e.*, property intended for occupation or for industrial or commercial use, let to third persons — the taxable income is the rent shown in the leases, provided it is normal, less 20 per cent for cost of upkeep, depreciation, etc. In the case of buildings occupied by their owners, the taxable income, or rather rental value, is estimated by comparison with similar properties in the neighbourhood which are actually let.

In the case of land, a distinction must be made between land which is leased and land which is not. If it is leased, the taxable income is the net income accruing to the lessor, less the amount normally estimated for the costs of upkeep, depreciation, etc., payable by him. If the land is not leased, the taxable income includes its rental value and the profits from its working. These are

determined as a rule by reference to the owner's accounts. If there are none or if they are not reliable, the assessment authorities take into account the book results of similarly worked property, the scale of rents and wages in various parts of the country and the income of the estate in question as recorded in the land register.

Special rules exist for assessing the income from vine-growing and from the felling of forests, woods and coppices, but mere mention of these is sufficient for our purpose.

Income from Trade and Industry. — Income of this class, which is taxable annually, is the income earned during the previous calendar year or during the last business period of twelve months ending before January 1st of the tax-year.

The taxable sum consists of gross profits, less only the business costs of earning and maintaining this income. These business costs are :

(1) Interest on borrowed capital invested in the enterprise and all charges, annual payments or royalties payable by the enterprise to third persons.

(2) Wages of employees and workmen and the emoluments and advantages representing the reward for services rendered.

From the profits of partnerships, general or limited, and of *de facto* associations are deducted the salaries or wages paid to any of the partners or to a co-owner as remuneration for services rendered. Percentages paid to a company's directors, managers, auditors, etc., are also regarded as deductible costs.

(3) General overhead expenses in connection with the upkeep, heating and lighting, etc., of the premises and equipment used in the business ; premiums paid for the insurance of the enterprise's buildings, equipment, furniture and stocks ; insurance contributions paid by the enterprise on behalf of the staff.

(4) Depreciation of equipment, furniture, machinery, tools, etc., in so far as such depreciation corresponds to actual depreciation during the period which the taxable profits cover. Although the amount of depreciation allowed will vary widely from case to case, speaking quite generally, it may be said that two per cent is allowed for buildings, five per cent for furniture, and ten per cent for machinery and plant.

(5) Losses sustained during the tax-year or period, provided they relate to operations by the enterprise.

(6) Expenditure occasioned by the repair, renewal or upkeep of buildings, plant and tools, provided this is current expenditure not covered by depreciation allowances and not calculated to improve the enterprise so as to add to its profits.

Non-deductible costs include the following :

(1) Cost of increasing personal or real property, of improving and enlarging the enterprise, redemption and repayment of debt, the establishment of reserve funds other than authorised redemption, and other similar expenditure ;

(2) Loss of income or capital incurred in previous years ;

(3) Taxes paid to the State and communes.

If the taxable income of the enterprise includes interest on Luxemburg bonds liable to coupon-tax, income-tax will be based on the total net income and the coupon-tax withheld at source will be deducted from it.

Income from Labour. — This includes salaries, wages, etc., and income from the liberal professions, literature, art and science.

The taxable income is the income for the previous calendar year, obtained by deducting from the taxpayer's gross professional receipts the cost to him of earning and maintaining this income. There are no special rules as to deductible costs in the case of the independent professions. These are determined with due regard to the custom of the particular occupation and by analogy with the rules in force for trade and industry.

Employees whose income does not exceed 35,000 francs are allowed to deduct from their salary a fixed sum of 2,500 francs as general professional expenses.

Deductions. — Before computing the tax, the following deductions are made from the total net income determined as above ;

(1) Interest and annuities on all kinds of debt, not already deducted at the time of determining net income, unless it is connected with an income which is not taxable as derived from a foreign source. This exception applies in particular to the case of a taxpayer who has contracted an interest-bearing debt for the purchase of real estate abroad.

If the taxpayer liable to pay interest or annuities of this kind is in receipt of income both from abroad and from the Grand-Duchy, the deduction will only be allowed up to an amount proportionate to the ratio between Luxemburg income and foreign income.

This rule applies both to taxpayers domiciled abroad and to persons living in the Grand-Duchy.

(2) Allowances legally due to the taxpayer's ascendant relatives, as well as allowances to his descendant relatives, if these allowances are taxed in the hands of their beneficiaries in the Grand-Duchy.

(3) The figure of 8,000 francs as a tax-free minimum.

(4) An allowance of 1,500 francs per descendant or ascendant relative dependent upon the taxpayer, on condition, however, that the latter's total income does not exceed 100,000 francs. All these deductions apply to surtax as well as to income-tax.

(5) With regard to surtax, taxpayers whose total income does not exceed 200,000 francs are entitled to an allowance of 30,000 francs.

(b) *Computation of Tax and Abatements.*

The law provides for no abatements and alleviations of the tax itself. All the allowances permitted are deducted from the amount taxable (see above).

Income-Tax. — The income-tax is on a graduated scale. Incomes are divided into thirteen slices, the first including the part of income between 8 and 12 thousand francs, and the last the amount over 700 thousand francs, and each slice of income is taxed at a certain rate. The scale varies from one per cent to nine per cent (see Annex).

If the taxpayer is in receipt of income that is not taxable in the Grand-Duchy (income from real estate abroad) or income that is not directly taxable in his hands (income from Luxemburg shares and bonds), account is none the less taken of this income in computing the tax on income upon which the taxpayer is liable. That is to say, the tax payable is computed by first fixing the average rate of tax that would apply if the non-taxable income were again liable and applying this rate to the income that actually is taxable.

As already mentioned, the income-tax is increased by "additional centimes" levied on behalf of the communes. These additional centimes are collected as a percentage of the principal tax, a percentage varying from commune to commune and year to year, according to budget requirements. For the year 1930-31, the additional centimes for the city of Luxemburg amounted to 130 per cent.

Surtax. — Surtax, as we have said, is collected on incomes the taxable amount of which (*i.e.*, net income less deductions and personal allowances) exceeds 30,000 francs. Incomes below 200,000 francs further enjoy a special allowance of 30,000 francs. The tax amounts to 60 per cent of what the income-tax would be if applied to the income liable to surtax.

Coupon-Tax. — This tax, when applied to interest on bonds issued by the State, public corporations and communes, is always 2 per cent, but when applied to the bonds of companies and private enterprises, it varies with the rate of interest; it is $3\frac{1}{2}$ per cent for interest not exceeding 4 per cent of the capital lent, and 4 per cent for interest above that rate.

B. COMPLEMENTARY TAX.

(a) *Computation of Taxable Property.*

The value of property liable to complementary tax is determined as follows :

(1) Land and buildings, mines, quarries, etc. (see page 309), and capital invested in trade or in commercial, industrial, agricultural, forestry and mining enterprises are reckoned at their market value on a fair appreciation.

(2) Cash and bank-notes in legal currency are assessed at their face value.

(3) Securities quoted on the Stock Exchange are assessed at the rate quoted on January 1st of the tax year, and other securities at their real value at the same date.

(4) All other debts are assessed at their nominal value, except doubtful or bad debts, which are reckoned at their real value only.

(5) The capital value of annual loans payable in perpetuity is reckoned at twenty-five times the annual sum. The value of life annuities is computed according to the age of the person at whose death the payment will cease and it varies between eighteen and three times the annual sum.

(6) The capital value of rights under a life insurance policy, whether a capital sum or an interest payment, is assessed at two-thirds of the total premiums or capital paid, unless the claimant proves what is the actual surrender value of the policy.

As regards foreign enterprises with establishments in the Grand-Duchy, the value of property liable to the complementary tax is determined, in the absence of other reliable data, by applying to their total property the ratio between their total income and the income on which they are liable to tax in the Grand-Duchy, and by considering as liable to complementary tax that part of the property corresponding to income taxable in the country.

Furniture, household stores and other articles for the personal use of the taxpayer and his family are always exempt from complementary tax. So are the mathematical reserves of insurance companies deposited with an official corporation.

As already mentioned, the tax is imposed upon taxpayers whose property exceeds 30,000 francs in value.

(b) *Computation of Tax and Abatements.*

Complementary tax is levied at a flat rate of 0.5 per thousand.

4. RETURNS, APPEALS AND COLLECTION.

Taxpayers' Returns.

Taxpayers with a total income of 10,000 francs or with property amounting to 50,000 francs or more in value have to make a return of their income or property to the Administration of Taxes during January of the tax-year on an appropriate form. In the case of companies and partnerships and taxpayers who keep accounts, the return must be accompanied by the balance-sheet and profit-and-loss account for the tax-year.

After a preliminary examination by the Administration, this return is submitted to a Board of Assessors (*Conseil de taxateurs*), which, in principle, sits in each commune and the members of which are recruited by Government from among communal taxpayers, half of them from a list prepared by the Administration, half from a list submitted by the communal council. The Board of Assessors may request the taxpayer to give verbal or written explanations of particulars in his return, may ask to see the accounts and order an expert examination to be made of them, either by the Administration or by an outside expert. The Board is also entitled, in principle, to demand all necessary information from public administrations, railway and insurance companies, etc. If the Board considers the return incorrect, it may alter it, but must inform the taxpayer of the figure it proposes to substitute for the figure given in the return, and specify its reasons for making the alterations, and at the same time invite the person concerned to submit his written or oral observations within a fortnight.

Omissions from returns are punishable with a fine of not more than twice the amount omitted if the omission was accidental, and not more than ten times if there was fraudulent intent.

Taxpayers who do not need to file returns are taxed on the basis of external evidence and by comparison with taxpayers in the same class.

Duties and Liabilities of Employers.

Persons or enterprises with workmen and employees in their service have to furnish in January a return giving the names and addresses of the various wage-earners in their employ and the wages paid to them during the previous calendar year (see also remarks under "Collection").

Appeals.

Taxpayers who fail to make their returns, even after receiving a form and a subsequent reminder by the Administration, are taxed *ex officio*, without right of appeal. The same happens when they fail to furnish the information and documents asked for by the Board of Assessors and if they refuse to submit their books and accounts for inspection.

Taxpayers who have complied with the law may appeal against the Board's decisions.

This they do by applying to the Administration within a month from the date of the demand note conveying the decision. The appeal is considered by a Council of Appeal sitting in each canton. Appeal against the Council's decisions may be made to the Appeals Committee of the Council of State within a month of their notification. Appeals against assessments do not warrant a suspension of payment.

Collection.

By Direct Payment. — Income-tax, surtax and supplementary tax are paid by the taxpayer personally.

The Boards of Assessors usually sit from May until October. The figures they fix are entered in a register, which serves as the basis for the collection lists sent to the tax-collectors. The latter then send a demand note to the taxpayer, who has to pay the whole amount due before March 31st of the following year; thereafter, interest is charged at 2 per cent.

By Deduction at Source. — Collection at source is reserved almost exclusively for the coupon-tax. The Government has not made use of its legal right to require that income-tax on salaries and wages shall be paid by deduction at source.

The law, however, itself provides that employers employing foreign wage-labour in the Grand-Duchy shall withhold from the wage for the first three months of employment the amount of tax corresponding to the annual remuneration.

Coupon-tax is withheld at the time of paying the interest on bonds issued by the State, communes and Luxemburg companies. It becomes payable in full on December 31st of the year which the interest covers and, if not paid by March 31st following, is liable to interest at the rate of 2 per cent per month.

PART II. — METHODS OF TAXING FOREIGN AND NATIONAL ENTERPRISES.

A. FOREIGN ENTERPRISES.

1. DEFINITION AND GENERAL PRINCIPLES.

For purposes of the present study, a foreign enterprise means any enterprise belonging to an individual or legal entity whose residence or fiscal domicile is not in Luxemburg. (For definition of these terms, see page 307.)

The law lays down that these persons, and consequently the enterprises belonging to them, are only liable to tax in respect of :

- (1) Income from commercial or industrial businesses situated or from capital of all kinds invested in the country, from the principal of such capital and from money employed in such businesses ;
- (2) Income and profits from trades and professions carried on in the country and from functions discharged in Luxemburg companies or in the service of other persons living in the country ;
- (3) Income from and the value of landed estate owned in Luxemburg.

The fiscal treatment of enterprises is the same whether they belong to individuals, to partnerships or to companies. Partnerships are taxable entities just as companies are, and both are taxed by the same means as individuals. The following rule is of importance, as it governs all income subject to tax in Luxemburg.

In the case of income-tax (and therefore surtax), the rate applicable to the taxable incomes of taxpayers who, along with this income, have other income not liable to tax is not the same as it would be if the taxpayer had taxable income only, but is a rate corresponding to the total of taxable and non-taxable income. But the tax due is obtained by applying this rate to the taxable income only.

Further, since the complementary tax on capital is closely associated with income-tax, we shall discuss, in connection with each class of income, the method of taxing, not only the income itself, but the capital from which it is obtained.

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) DIVIDENDS.

Dividends are subject — as, in principle, is all other income — to income-tax and, in certain circumstances, to surtax, and the value of the shares of all kinds on which they are paid is liable to the complementary tax.

It is the law's intention that income or capital which has been taxed against a company shall not be taxed again in the hands of the shareholders to whom this income and capital ultimately accrue or belong.

Consequently, a foreign enterprise which has Luxemburg shares in its portfolio will not itself pay tax on these dividends and shares. But if the enterprise is liable, not only in respect of this income, but on other income, such as industrial or commercial profits or income from landed estate, the authorities responsible for determining the rate of tax to be applied to the taxable income will take account of the whole income, including these dividends. This does not, of course, apply to complementary tax, which is a proportional tax and not, like income-tax, a graduated one.

If a foreign enterprise has an establishment in the Grand-Duchy which has foreign shares in its portfolio, the enterprise itself must pay income-tax and complementary tax on the dividends from and value of these shares. The exemption in favour of Luxemburg dividends and shares does not apply in this case, since the capital and income have not already been taxed against the foreign company issuing the shares in question.

In the case we have been considering, the foreign dividends and shares have not been taxed as income from or investment of capital, but as income and capital belonging to a trade or industry. If, therefore, a foreign enterprise which has no establishment in the country merely receives dividends in Luxemburg from a non-Luxemburg company, no tax is due.

Further, the various privileges and exemptions granted to Luxemburg holding companies do not apply to similar foreign companies.

(b) INTEREST.

(1) *Interest on Bonds.* — Interest on bonds issued by the State, public corporations and by Luxemburg enterprises and companies is subject to a special tax called the "coupon-tax", which, unlike other taxes, is withheld at the source by the person who owes the interest. This interest is always subject to coupon-tax, irrespective of the recipient's domicile, so that foreign enterprises in the possession of these bonds are in all cases liable to coupon-tax.

This tax takes the place of income-tax and complementary tax, but not of surtax. But, as the latter is only payable in cases when income-tax is payable, foreign enterprises which have no other taxable income in the Grand-Duchy are liable under this head to no other tax than coupon-tax.

It is otherwise if the company has a Luxemburg establishment which has in its portfolio bonds liable to coupon-tax. In this case, the company has to pay income-tax on all its Luxemburg income, including interest on bonds, at the rate corresponding to its total income (foreign and Luxemburg), but from the tax as thus assessed is deducted coupon-tax already paid at the source.

Surtax is fixed on the same bases, but after first deducting 30,000 francs.

(2) *Interest on Secured Loans.* — The interest and principal of loans secured on a mortgage or other security on real property legally situated in the Grand-Duchy are subject to income-tax and complementary tax, respectively, whatever the domicile of the debtor and creditor.

(3) *Interest on Unsecured Loans.* — The interest and principal of debts contracted by an individual or legal entity resident in the Grand-Duchy are, as a rule, taxable in the hands of the creditor, whatever his domicile. The Administration may require the debtor to pay the tax due on the interest in the name and on behalf of his creditor.

The rule for taxing interest owing by Luxemburg nationals to foreign credit institutions raised a controversy which was settled by the following decision :

Income consisting of interest on sums advanced by a foreign financial institution to Luxemburg nationals is not regarded as income of an enterprise operated in the country by a foreign company, if this establishment has no branch, agency or representative in the Grand-Duchy and if the operation was an isolated or accidental one. Nor are such advances regarded as investments of capital in Luxemburg, if the contract was concluded and is executable abroad.

(c) DIRECTORS' PERCENTAGES.

The percentages distributed by companies to their directors represent for these companies an item of cost which they may deduct from their profits. These percentages, when distributed by Luxemburg companies, are in all cases taxable in the hands of the beneficiary, whatever his domicile.

The rate of tax is determined by the taxpayer's total income, both Luxemburg and foreign. In practice, the Administration employs the intermediary of the company to which the director belongs; a demand note is sent through the company and the tax is paid, in the usual way, by the taxpayer himself.

Directors' percentages distributed by foreign companies to persons resident in the Grand-Duchy are taxable there. Further, a foreign company liable to Luxemburg tax may not deduct from its taxable profits all or part of the percentages paid to its directors unless those percentages are themselves liable to tax in the Grand-Duchy.

Instead of the two rules — taxation at the enterprise's real centre of management and taxation in the fiscal domicile of the beneficiary (their simultaneous application means double taxation) — the Convention with Belgium provides for taxation at the enterprise's centre of management only.

(d) ROYALTIES FOR USE OF PATENTS, COPYRIGHTS, TRADE-MARKS, SECRET PROCESSES AND FORMULÆ AND SIMILAR INCOME.

Royalties for the use of patents, copyrights and other incorporeal property rights are not as a rule taxable when paid to persons not resident in the Grand-Duchy. This rule does not apply to royalties which are paid to an enterprise with an establishment in the Grand-Duchy and included among the establishment's receipts.

The capital value of these incorporeal property rights will only be liable to complementary tax if the patents, copyrights, etc., are part of the assets of an establishment situated in Luxemburg, whether they are exploited by the establishment itself or by third parties to whom the latter has ceded them.

(e) RENTS FROM REAL ESTATE, MINING ROYALTIES AND SIMILAR INCOME.

Income from real estate, of whatever kind, is always taxable if it is obtained from property situated in the country. The same applies to the value of the property, property rights and concessions to which the income corresponds.

Income-tax is levied at the rate corresponding to the taxpayer's total income (from Luxemburg and from foreign sources).

(f) GAIN DERIVED FROM THE PURCHASE AND SALE OF REAL ESTATE, SECURITIES AND PERSONAL PROPERTY.

The rule is that purchase and sale transactions are only taxable if they are in connection with the exercise of a trade or industry or if, although isolated transactions, they are in the nature of acts of speculation.

Thus, if a foreign enterprise has an industrial or commercial establishment in the Grand-Duchy, all the profits from any purchases or sales whatever by such establishment are taxable, even when the operation is not directly connected with the ordinary business of the establishment. But if the enterprise has no establishment in the country and purchases and sales are purely isolated transactions having no counterpart in the Grand-Duchy, no tax will be imposed.

(g) SALARIES, WAGES, COMMISSIONS AND OTHER REMUNERATION FOR SERVICES.

The remuneration of workmen and employees working in the Grand-Duchy are taxable, even if the latter are living abroad.

This ruling is confirmed by the Belgo-Luxemburg Convention, although an exception is made in favour of workers living in the frontier zones. The latter only pay State taxes in the country where they have their fiscal domicile. The salaries of public officials and employees and public and private pensions are always taxable in the country which pays them.

The law requires that employers who employ foreigners shall, during the first three months of the latter's employment, withhold the tax payable on their annual salaries or wages. Moreover, as we said in Part I, employers have to furnish a yearly list of the workmen and employees in their service with the salary or wage paid (this list includes Luxemburg and foreign salaried workers and wage-earners). But though the law allows the Government to order the collection of income-tax on salaries and wages by deduction at source, this method of collection is applied only in the case of foreigners.

As regards professions which involve personal services, but which are carried on independently, income-tax is only payable if the persons concerned exercise their calling in the country in some periodical manner.

The Belgo-Luxemburg Convention adds to this condition the existence of a permanent establishment for the exercise of the profession or calling.

Commercial travellers in the employ of foreign companies are not liable to tax on the mere ground that they visit the Grand-Duchy. Administrative practice, in fact, holds that commercial travellers travelling for foreign companies are only liable to tax in the Grand-Duchy if they live there. It may be added, although this is not immediately relevant to the present issue, that this fiscal obligation exists even if the commercial traveller pursues his work abroad, while commercial travellers employed by Luxemburg companies are liable to tax in the Grand-Duchy (except those living in Belgium), even if they live and work abroad.

(h) INCOME FROM A TRUST.

Luxemburg law takes no cognisance of trusts and we need not therefore concern ourselves with the taxation of these estates.

(i) INCOME FROM CARRYING ON A BUSINESS OR INDUSTRY.

The law does not strictly define the cases when a foreign enterprise which operates in the Grand-Duchy is taxable there. According, however, to jurisprudence and administrative practice, a foreign person or enterprise becomes liable to tax in the Grand-Duchy as soon as such person or enterprise settles in the country or establishes employees and equipment there in any form and for any considerable length of time, with a view to exercising a trade or industry in the country.

It follows from this general principle that :

(1) An enterprise which carries on business in Luxemburg only through a *local commission agent* or a *broker* is not liable, since these intermediaries cannot be described as the enterprise's employees.

(2) The same applies, in principle, to a *local dealer* or *distributor*. But if this dealer or distributor is bound to sell only the products of the enterprise, the Administration might regard him as really nothing more than the enterprise's servant and might therefore tax the foreign enterprise.

(3) If a foreign enterprise employs a *travelling salesman* to visit its customers in the Grand-Duchy (*whether he has power to conclude a contract or not*), the enterprise will not be liable, for

it cannot be said to possess works or an establishment in the Grand-Duchy. Moreover, the commercial traveller, unless he lives in Luxemburg, is not liable in respect of the remuneration he receives from the enterprise.

(4) If an enterprise does business with the Grand-Duchy through a *local agent with a power of attorney*, the real position of this agent towards the enterprise must be determined. If he is merely the employee of the enterprise, the latter must be regarded as having an operating centre in the Grand-Duchy and, as such, liable to Luxemburg tax.

(5) If a foreign enterprise is represented in the Grand-Duchy by an *agent selling out of a stock* entrusted to him, the enterprise will be liable, not only to income-tax on the profits from sales, but to complementary tax on the capital value of the stock.

(c) Foreign enterprises which have a *permanent establishment* in the Grand-Duchy are liable to tax there. Even if there is no permanent establishment, a foreign enterprise may be taxed if it establishes its equipment in the Grand-Duchy with an industrial or commercial purpose in view ; this applies particularly to building contractors.

The Convention with Belgium contains no departures from the foregoing rules. It merely defines here certain terms. Thus, permanent establishments must be understood to include real centres of management, branches, factories, workshops, agencies, shops, offices and warehouses. The fact that an enterprise established in one of the two contracting States has business relations with the other through some really independent agent or company (broker, commission agent, subsidiary, etc.) does not imply that the enterprise has a permanent establishment in the latter country.

B. NATIONAL ENTERPRISES.

By national enterprises are to be understood enterprises belonging to persons who have their residence or fiscal domicile within the Grand-Duchy.

These enterprises are liable to tax in respect of all their income and property, whether situated abroad or in Luxemburg. The only exemptions are in favour of income from real property abroad, which is exempted by the income-tax law itself and the exemption in the Belgo-Luxemburg Convention, whereby " industrial, mining, commercial or agricultural enterprises are taxable in each of the two States in proportion to the income earned by permanent establishments in the country ". (See also the references to holding companies on page 325.)

The method of applying this principle calls for a few observations.

Direct taxes paid abroad on foreign-earned income are deducted from the sum taxable in the Grand-Duchy.

Income-tax and complementary tax on, respectively, the dividends from and capital value of foreign shares are paid by the owner of the dividends and shares — contrary to what happens in regard to Luxemburg shares.

The coupon-tax is not, in principle, applied to foreign bonds. Accordingly, interest on these bonds and their capital value, respectively, are subject, like all other income and capital, to income-tax and complementary tax.

Further, income from real estate abroad, although not taxed in the Grand-Duchy, is taken into account when fixing the rate of tax applicable to other taxable income.

The general rules for the taxation of foreign income and capital, together with these few remarks, make it unnecessary to review in detail the fiscal regime of the various kinds of income which Luxemburg taxpayers may derive from abroad.

PART III. — METHODS OF ALLOCATING TAXABLE INCOME.

A. FOREIGN ENTERPRISES WITH LOCAL BRANCHES OR SUBSIDIARIES.

I. GENERAL QUESTIONS AND METHODS OF APPORTIONMENT.

(a) BOOK-KEEPING AND ACCOUNTING REQUIREMENTS.

With regards to taxpayers engaged in trade or industry, Article 9 of the Income-Tax Law says : " in the absence of reliable accounts or of continuous inventories and balance-sheets, profits and gains shall be estimated by tax assessors ". Article 34 prescribes that associations with a legal entity (and this rule has been extended in practice to all traders who keep accounts) shall accompany their tax returns by their latest balance-sheet and profit-and-loss account and by any other documents that will serve to determine their taxable income. The same article adds that foreign companies must, in addition to the balance-sheet and profit-and-loss account of their dealings in the Grand-Duchy, furnish similar documents with reference to the whole of their operations. Failure to comply with the provisions of Article 34 entails taxation *ex officio* (subject, of course, to other purely penal sanctions).

Except, however, for the rule concerning continuity of balance-sheets and inventories, fiscal law and jurisprudence do not of themselves determine how books and accounts shall be kept. Reference must be made for this matter to the rules contained in the Commercial Code and established by commercial practice.¹

Jurisprudence also decrees that, in the event of taxation by estimate or *ex officio*, assessment shall be based upon " factors fairly selected so as to show the relative importance or business operations of the different establishments ".

(b) METHODS OF ALLOCATION.

In addition to the rule set forth at the end of the previous heading, the two leading principles which govern the allocation of profits of foreign enterprises are (a) the rule resulting from Articles 9 and 34, read in conjunction — namely, that the normal basis of taxation is the enterprise's accounts and (b) the rule laid down in Article 26, which says that income ascribable to the Luxemburg branch of a foreign enterprise " shall represent a fraction of the total net income not less than the proportion between general overhead expenses or manufacture, or capital invested, or the wage-bill,

¹ The books prescribed by Articles 8 to 11 of the Commercial Code are the following : the day-book, in which are entered up day by day in chronological order all operations effected by the taxpayer in the conduct of his business ; the inventory book, containing copies of the inventory of assets and liabilities which the taxpayer is required to establish annually ; the letter book, containing copies of all letters despatched. All these books and the originals of all incoming letters must be kept for ten years.

or any other factors fairly selected so as to show the relative importance or business operations of the different establishments ”.

As regards the allocation of assets liable to complementary tax, the law has decided that, failing satisfactory evidence, assets taxable in the Grand-Duchy shall be determined on the basis of the ratio between the taxable income and the total income of the foreign enterprise, but in most cases the Administration possesses sufficient data so as to be able to estimate directly the assets and liabilities of the Luxembourg branch.

1. Method of Separate Accounting.

Whenever the Luxembourg branch of a foreign enterprise can submit accounts and documentary evidence in proper form, the Administration examines the documents and the books to see whether the accounts tally with the real position and results of the Luxembourg part of the enterprise regarded separately.

The authorities will, of course, check the accuracy of the entries concerning operations with third parties, but will pay special attention to the transactions and accounts of the establishment with the parent enterprise and to comparing results in Luxembourg and abroad.

It will therefore examine whether all expenses and charges deducted from the Luxembourg income really refer to business done in the Grand-Duchy and, if these deductions include part of the general overhead expenses and interest charges of the enterprise's head office abroad, it will only allow such expenses and charges to be taken into account if they have been incurred on behalf of the Luxembourg branch. Further, jurisprudence has decided that Article 41, whereby an employer may only deduct wages declared in the return made on the wage-earners' behalf, also covers salaries and wages paid by the parent firm on behalf of its branch.

The official responsible for assessment will also check the prices at which goods have been invoiced to the branch by the parent enterprise or, conversely, the sums debited as interest on loans, advances, royalties and commissions paid on behalf of the parent enterprise. The purpose of this examination is to see whether the various transactions between branch and parent were effected under the same conditions as between two separate enterprises and to make sure that these operations and the book entries concerning them do not conceal a transfer or displacement of taxable income.

If inaccuracies can be easily located, they will simply be corrected, and the Administration will, for the rest, abide by the accounts.

If not, recourse will be had to an empirical method or to the method of fractional apportionment.

The former will be adopted if the discrepancy between the declared results of the foreign enterprise's Luxembourg branch and the results of similar national enterprises relates only to the amount of net profit ; fractional apportionment will be employed if the difference relates to both net and gross profits.

2. Empirical Methods.

Owing to the diverse operations of industrial enterprises, the empirical method can rarely be employed to allocate either their profits or their capital ; this method is therefore most often reserved for commercial undertakings.

Before taxable profits can be assessed empirically, the Administration must know either the exact amount of purchases effected by the taxable establishment and the cost price of the goods bought, or the establishment's exact turnover. Further, the profits normally obtained by the establishment's branch of trade must be ascertainable from data supplied by the accounts of similar national enterprises. There is no official scale of such profits and the inspector responsible for assessing tax fixes them for each year.

3. *Method of Fractional Apportionment.*

This method is mainly applied to industrial enterprises, to which, as we have said, the empirical method is rarely suited.

The use of this method is governed by Article 26 of the Law, which says that the income taxable against the Luxemburg branch of a foreign enterprise " must represent a fraction of the total income not less than the proportion between general overhead expenses or production, or capital invested, or the wages paid or any other factor fairly selected so as to show the relative importance or business operations of the different establishments ".

The choice of the factors to be considered for purpose of allocation by the fractional method is not governed by law, practice or jurisprudence. The basis is fixed for each separate case according to the kind of enterprise and the possibility of checking a particular factor.

Fractional apportionment is invariably employed for foreign insurance companies and, under the separate heading devoted to these enterprises, we shall see how it works.

(c) APPORTIONMENT BETWEEN BRANCH AND PARENT ENTERPRISE.

1. *Apportionment of Gross Profit of Local Branch to Real Centre of Management abroad.*

The question of allocating part of the gross profits of a branch in the Grand-Duchy only arises if the branch's receipts originate in part in operations effected by the foreign head office or in goods supplied by the latter. These questions will be considered under the headings of allocation of liabilities and application of the methods of allocation to industrial and commercial enterprises.

2. *Apportionment of Expenses of Real Centre of Management to Branch.*

Interest Charges.

As regards debts contracted by the head office abroad, interest may only be deducted if it is in respect of loans contracted on behalf of the taxable branch or in respect of capital allotted to that branch.

General Overhead.

General overhead expenses of the real seat of management may only be deducted from the profits of the Luxemburg branch if they were incurred on that branch's behalf.

In the case of salaries and wages, it is further necessary that they shall have been taxed in the Grand-Duchy.

3. *Apportionment of Net Profit of Branch to Deficitary Parent or vice versa.*

If the Luxemburg branch of a foreign enterprise has realised a profit while the rest of the enterprise has operated at a loss, the latter is never taken into account when determining the branch's profit, even when other methods than that of separate accounts are used.

If the Luxemburg branch sustains a loss, while the rest of the enterprise realises a profit, preference is given to the method of fractional apportionment, unless, however, the deficit of the branch appears genuine and not as a displacement or transfer of profits.

(d) APPORTIONMENT BETWEEN PARENT ENTERPRISE AND SUBSIDIARIES.

The same methods of allocation are applied to subsidiaries as to branches, including the methods

of fractional apportionment and empirical methods. The basis for this practice is found in the following rule of jurisprudence :

“ A company is not exempt from taxation in the Grand-Duchy if, in order to do commercial or industrial business in Luxemburg, it creates a new company in that country, retaining over it such a preponderant influence that the new company is reduced to the rôle of an agent responsible for securing the success of the foreign enterprise's business.”

II. APPLICATION OF THE METHODS OF ALLOCATION IN SPECIFIC CASES.

(a) INDUSTRIAL AND COMMERCIAL ENTERPRISES.

I. *Selling Establishments.*

The destination of goods sold by an enterprise or establishment which is taxable in the Grand-Duchy is of little importance. From the fiscal standpoint, it is the same thing whether the foreign enterprise's branch sells in Luxemburg or sells abroad.

The essential point is to ascertain the profits derived from the activities of the taxable establishment's business — *i.e.*, from its sales. Accordingly, when that establishment receives goods which it sells on behalf of its parent enterprise abroad, it has to be determined whether the prices at which these goods are invoiced are the same as the prices at which they would have been invoiced against a Luxemburg establishment working under the same conditions. If there is no way of determining this, the taxable profit will be calculated on the basis of the establishment's turnover, to which will be applied a coefficient representing the net profit, this coefficient being fixed by comparison with the position of Luxemburg enterprises working under similar conditions.

2. *Manufacturing Establishments.*

The normal profit of mines, factories, yards, workshops, etc., maintained in Luxemburg by a foreign firm is the profit resulting from the operations of these establishments and plants and, in principle, it coincides with the profit of similar Luxemburg enterprises.

If it is impossible to determine the taxable profit by the method of separate accounting — and it frequently is — this profit is assessed empirically or by fractional apportionment.

If the foreign enterprise has only commercial establishments abroad, the method of fractional apportionment can only be used if there is some common denominator for the Luxemburg and foreign parts of the enterprise. Otherwise, the only means of assessing profits will be by comparison with Luxemburg enterprises engaged in the same kind of industrial business.

If the foreign enterprise has industrial establishments both in the Grand-Duchy and abroad, the method of fractional apportionment is employed, and choice is made of the allocation factors which seem best suited to the nature of the enterprise — *viz.*, production, general overhead expenses, invested capital, wages, etc.

3. *Processing Establishments.*

What was said above concerning the normal taxable profit and the use of the fractional apportionment method in connection with manufacturing establishments applies also to processing establishments.

4. *Buying Establishments.*

Buying establishments, like all the other industrial or commercial establishments of a foreign

enterprise, are taxable on the basis of their business profits, and their normal profit can be computed from the profits accruing to a Luxemburg enterprise which buys on behalf of a foreign enterprise and operates under conditions similar to those of the establishment in question. Thus, if the method of separate accounting is inapplicable, recourse will be had to an empirical method.

5. *Research or Statistical Establishments, Display Rooms, etc.*

Research or statistical establishments, display rooms, etc., which a foreign enterprise owns in the Grand-Duchy, are not as a rule taxable. There must, however, be absolutely no intervention in the affairs of the enterprise and any share in business, direct or indirect, would afford grounds for taxation.

(b) BANKING ENTERPRISES.

Hitherto, foreign credit institutions with branches in the Grand-Duchy have been taxed on the basis of the separate balance-sheets supplied to the fiscal Administration in respect of Luxemburg establishments.

(c) INSURANCE ENTERPRISES.

Jurisprudence has decided that foreign insurance companies are taxable in the Grand-Duchy on the share of the total net profits from business done in Luxemburg corresponding to the ratio between the total receipts of this kind and Luxemburg receipts. Before this ratio can be determined, we must know what makes up the net profits from operations of the same kind as those affected in the Grand-Duchy. And this necessitates first ascertaining the gross profits from these operations.

There is no difficulty in doing this in the case of gross business profits — *i.e.*, the profits resulting from the excess of receipts over payments to insured persons.

But gross profit from investments is another matter, for the funds of an insurance company are amalgamated. In order, therefore, to determine what share of the interest received by a company represents a given class of insurance, it has been decided that interest from investment shall be allocated in the same way as interest paid to insured persons, excepting, however, sums distributed out of profits. Having fixed the gross business profit and the profits from investment in the case of insurance branches which have concluded policies in the Grand-Duchy, it is next ascertained how much must be deducted from these gross profits in the way of general overhead expenses, in order to furnish the total net profit.

There is no general rule for the allocation of general overhead expenses with a view to this deduction; some more or less empirical ratio is chosen according to the circumstances of the case.

From the total net profit of the insurance branch in the Grand-Duchy, as thus determined, is then deducted its share of general overhead expenses. And the sum taxable in the Grand-Duchy is finally obtained by applying to the net profit thus determined the ratio between the total receipts pertaining to this profit and the receipts collected in the Grand-Duchy.

(d) OTHER KINDS OF ENTERPRISES.

In the case of transport enterprises, electric enterprises, telegraphs, telephones and mining enterprises, profits are normally apportioned on the basis of the separate accounts of the Luxemburg and foreign establishments (see page 321). If there are no separate accounts or if they do not accurately reflect the business of the Luxemburg establishment, the taxable sum will be fixed by fractional apportionment. The following are a few illustrations of how this method is applied.

Transport Enterprises. — The case has not yet arisen and therefore no practical example can be given. According to the rule laid down in Article 26 of the Law, whereby the share of profits to be ascribed to the Luxemburg establishment must not fall below the proportion between the various cost factors, allocation must be based on the chief expenses of this form of enterprise — such as upkeep of vehicles, salaries, wages, etc.

Power, Light and Gas Companies. — The chief item of costs to be taken into account as an allocation factor is the upkeep of systems. Apportionment may also be based on length of systems, etc.

Telegraph and Telephone Companies. — Telephones and telegraphs are operated exclusively by a public service which is exempt from tax. Therefore no question of allocation arises.

Mining Enterprises. — In virtue of the oft-repeated principle that allocation by fractional apportionment is based upon cost, these enterprises are assessed either according to the cost of extraction or according to the quantities (and qualities) extracted from the different mines.

B. NATIONAL ENTERPRISES WITH BRANCHES OR SUBSIDIARIES ABROAD.

The question of allocating the profits and capital of national enterprises with branches or subsidiaries abroad does not normally arise, since the latter are in all cases liable in respect of all their income (except income from real estate abroad) and of all their property (except real estate abroad), while tax is applied to foreign income at the same rate as to income earned in Luxemburg.

In the case, however, of enterprises with establishments or branches in Belgium, Article 4 of the Belgo-Luxemburg Convention provides as follows :

“ Industrial, mining, commercial or agricultural enterprises are liable to tax in each country in proportion to the income earned by permanent establishments ¹ in the country.

“ If there are no accounts which show this income regularly and separately, the competent administrations in the two countries shall jointly draw up rules of allocation.”

No such rules have as yet been fixed.

Furthermore, negotiations are in progress with France and Germany. No agreement has yet been concluded with France, but, as regards Germany, it has been decided that, until the proposed Convention is ratified, enterprises in each country which have an establishment in the other country shall be treated according to the rules laid down in the old agreements (now lapsed) concluded with Prussia in 1909 (*Memorial of the Grand-Duchy*, 1909, No. 50) and with Hesse in 1913 (*Memorial of the Grand-Duchy*, 1913, No. 29). Both these Conventions lay down that establishments are liable to tax in the country where they are situated and that profits shall be allocated in proportion to the capital invested in each country.

C. HOLDING COMPANIES.

There are no special rules for foreign holding companies with shares in Luxemburg companies and, as a rule, they, like other shareholders, are exempt from income-tax and complementary tax, it being the law's intention that dividends and shares on which a company has already paid tax as income from capital shall not again be taxed in the hands of shareholders. Similarly, interest on bonds accruing to such holding companies is subject to the ordinary rules applying to coupon-tax.

¹ For the meaning given to “ permanent establishment ” in this Convention, see page 319.

In the case, however, of Luxemburg holding companies, the law provides for certain exemptions and a special regime. These companies are exempt in respect of their own income from income-tax, complementary tax, the communal centimes and surtax.

Exemptions from the first two of these taxes is an exception to ordinary law, for, although ordinary companies are not liable to income or complementary tax on dividends from and the capital value of Luxemburg shares in their portfolio, they are liable to both these taxes in respect of their foreign dividends and shares.

Nevertheless, the fact that Luxemburg shareholders are thus in possession of shares and dividends, some of which are of foreign origin and have not been taxed in the Grand-Duchy, is duly taken into account, and the shareholders are held liable to income-tax and complementary tax on that part of their dividends and shares which represent foreign investment.

The exemption from "additional centimes" tax and surtax is an obvious exception to the ordinary law.

Holding companies are not exempt from coupon-tax on bonds in their holding. The reason for this is that this tax is deducted at the source and there are no rules permitting its refund to these companies. On the other hand, bonds issued by holding companies are free of coupon-tax and their holders receive interest without deductions of any kind.

Annex.

TABLE OF TARIFFS.

I. INCOME TAX.

Taxable income (In francs)	Tax-rate applying to income between the two figures in left-hand column (Percentage)	Amount of tax on the higher of the two income figures in left-hand column (In francs)
Up to 8,000	—	—
8,000— 12,000	1.0	40
12,000— 20,000	2.0	200
20,000— 35,000	3.0	650
35,000— 60,000	4.0	1,650
60,000—100,000	5.0	3,650
100,000—150,000	5.5	6,400
150,000—200,000	6.0	9,400
200,000—300,000	6.5	15,900
300,000—400,000	7.0	22,900
400,000—500,000	7.5	30,400
500,000—600,000	8.0	38,400
600,000—700,000	8.5	46,900
700,000 and over	9.0	

II. SURTAX.

Taxable Sum.

1. A taxpayer whose income does not exceed 200,000 francs is liable to surtax on the amount of his income subject to income-tax, less 30,000 francs.

2. A taxpayer whose income is over 200,000 francs is liable to surtax on the amount subject to income-tax without any deduction.

Rate of Tax.

Sixty per cent of the income-tax rate on the same taxable sum.

III. COUPON TAX.

	Percentage of the income
Bonds issued by the State and communes	2.0
Bonds issued by Luxemburg companies, the interest on which is 4 per cent or less	3.5
Bonds issued by Luxemburg companies, the interest on which exceeds 4 per cent, and bonds issued by foreign legal entities, enterprises and companies	4.0

IV. COMPLEMENTARY TAX.

0.5 per thousand of the value of the taxable property.

NETHERLANDS

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PART I. — GENERAL DESCRIPTION OF THE INCOME-TAX AND PROPERTY-TAX SYSTEM ¹

The following are the taxes which the Netherlands Government imposes more or less regularly upon income and property :

The land and buildings tax (*grondbelasting*) ;

The tax on dividends and *tantièmes* (*dividend- en tantiëmebelasting*) ;

Taxes on income : *i.e.*, income tax proper (*inkomstenbelasting*) ; and " Communal Fund tax " (*gemeentefondsbelasting*) ;

Taxes on property : *i.e.*, property tax proper (*vermogensbelasting*) and Defence Tax No. I (*verdedigingsbelasting* I). There was also a Defence Tax No. II, which was a tax on income, but it was abolished in 1930. ²

The *land and buildings tax* is an impersonal tax. It is imposed upon the income from lands and buildings situated in the Netherlands irrespective of whether the taxable property belongs to an individual, a legal entity or an association having no legal entity and of whether the owner is or is not domiciled abroad.

The *tax on dividends and tantièmes* is principally levied upon the net profits of Netherlands share companies, even if derived from real property situated in the Netherlands ; profits, however, are taxed only on distribution. It does not matter whether the recipients of this income are resident in the Netherlands or not ; nor does the law distinguish between distributions to individuals and those to legal entities. There exist, however, special provisions with a view to preventing the

¹ Legislation in force on May 1st, 1933.

² The relative importance of these taxes is shown by the following table based on the Ways and Means estimates of the National Exchequer (1932), of the Loan Fund (1932) and of the Communal Fund (1932-33) (May 1st-April 30th).

Unless otherwise stated, the principal of the tax mentioned below accrues to the National Exchequer and the " additional cents " mentioned below to the Loan Fund.

	Florins
Land and buildings tax, the principal of which is 23,260,000 florins, and three-quarters of this amount goes to the communes in which the property is situated ; the remaining quarter for the State amounts to	5,815,000
Plus 4,652,200 florins " additional cents "	4,652,200
Tax on dividends and <i>tantièmes</i> (including 5 million florins of " additional cents ")	20,000,000
Income tax (including 14,900,000 florins of " additional cents ") . .	89,900,000
Tax on behalf of Communal Fund (part accruing to the Communal Fund)	75,000,000
Property tax (including 14,500,000 florins of " additional cents " , 6,800,000 florins of which accrues to Communal Fund)	28,500,000
Defence Tax No. I (all accruing to the Loan Fund)	16,000,000
Total	239,867,200

Allocation of yield from above taxes: National Exchequer, 109,815,000; Loan Fund, 48,252,000; Communal Fund, 81,800,000 florins.

Other revenue accruing to the Exchequer and to the Loan Fund from stamp duties, registration fees, death duties, etc., excise taxes, etc., Customs duties, etc., 305,140,000 florins.

dividends received by a company from being taxed a second time when distributed along with the company's other profits.

The law confers upon a company no claim against its shareholders, directors, etc., on the grounds that it has paid the tax on dividends and *antièmes*.

Foreign companies are not liable to this tax, but, unlike Netherlands companies, are liable to the income and property taxes imposed respectively on the profits they earn in the Netherlands and on capital they invest in the country.

The *income taxes* are levied on :

- (a) The total net income of individuals living in the Netherlands ;
- (b) The profits which foundations domiciled in the Netherlands would derive from enterprises they may exploit ;
- (c) Netherlands income accruing to individuals resident abroad or to foreign legal entities.

The *property taxes* are levied on :

- (a) The total property of individuals living in the Netherlands ;
- (b) Property in the Netherlands owned by individuals resident abroad and capital invested in the Netherlands by foreign legal entities.

I. LAND AND BUILDINGS TAX. ¹

The tax is payable by individuals, legal entities, and associations of all kinds even without legal entity, who enjoy real property in the Netherlands in virtue of a right, such as ownership, usufruct, long-term lease (*emphytéose*), etc.

The tax is levied annually according to the circumstances existing on January 1st at a *pro rata* rate of the cadastral income from land and buildings in the Kingdom as such income exists on January 1st. The cadastral income is determined with reference to the position applying to land in 1879 or so and to buildings in 1894 or so.

The rate is fixed at 6 per cent and 4.86 per cent of the cadastral income, for lands and buildings respectively, and additional *cents* are levied on behalf of the Loan Fund (20), ² the province (maximum 50) and the commune (maximum 20 in the case of land, 80 in the case of buildings).

Land newly dyked, drained, brought into cultivation, etc., is granted a temporary exemption of evaluation or re-evaluation. Churches are exempt and so are certain other public buildings.

The tax is assessed by the controller of land and buildings tax without any return being made by the taxpayer. It is paid by the latter in a number of equal monthly payments, the first being due at the end of the month following the notice of assessment, the last at the end of the tax year, subject to the requirement that there never should be less than five in number.

It is only when the measurement or the evaluation of the taxable property is made for the first time, or when this is again done in the cases determined by the law, or when the administration has neglected to do so in such cases, that the taxpayer is entitled to appeal on such grounds before the provincial Government. Except in the case of neglect on the part of the administration, this

¹ Legislation : Wet van 26 Mei 1870 (*Staatsblad*, No. 82) tot regeling van de grondbelasting (Law of May 26th, 1870, *Staatsblad*, No. 82, concerning land tax). Wet van 31 December 1892 (*Staatsblad*, No. 315) regelende het tarief van de grondbelasting voor de ongebouwde eigendommen en wet van 15 Juli 1907 (*Staatsblad*, No. 203) regelende het tarief der grondbelasting voor de gebouwde eigendommen (Law of December 31st, 1892, *Staatsblad*, No. 315, relating to the land-tax tariff for lands, and Law of July 15th, 1907, *Staatsblad*, No. 203, relating to the tariff of the land tax applicable to buildings).

The Law of May 21st, 1931 (*Staatsblad*, No. 203), temporarily exempts land reclaimed from the Zuyder Zee.

² From the year 1933 lands are exempted from the additional *cents* for the loan fund.

appeal must be made after the taxpayer has been notified of the results of these operations, the notification being made before the tax is assessed.

Appeals on grounds other than measurement or evaluation must be carried within two months of the tax notice to the provincial Government.

II. TAX ON DIVIDENDS AND TANTIÈMES.¹

I. TAXPAYERS.

According to the conception underlying Netherlands Law, the tax on dividends and *tantièmes* is not, strictly speaking, a direct tax. It is a tax levied on acts — *viz.*, the distribution of profits each time they take place, whether several times a year or at long intervals. These acts are only taxable when accomplished by certain categories of persons. If these persons are called taxpayers, one may say that the taxpayers are share companies, limited partnerships with share capital, co-operative and other societies and mutual insurance companies established in the Netherlands (Article 1 of the Law). Circumstances must decide whether a share company, etc., is established in the Netherlands (same article). In other words, the place of the taxable act is the place where the company is *de facto* domiciled.

Profits are not distributed unless they pass from the possession of the company into that of some other person. Accordingly, the tax will never be owing by an association which has no estate entirely separate from that of its members, as in the case of a *partnership*. The latter, moreover, has no legal entity, and its creditors, although, in the event of the winding-up of the partnership's assets, they have a prior claim over the partner's personal creditors, are in reality but creditors of the partners. Thus neither the law on the taxation of dividends and *tantièmes* nor the laws relating to income and property taxes deal with partnerships. The same applies to similar foreign associations, even if the law under which they were constituted has vested them with a legal entity, the only question being whether the profits accrue to the partners directly or not.²

The fiscal treatment of partnerships and their members applies also to *limited partnerships* and to those of their members who are jointly and severally liable. (Limited partners, on the other hand, pay income tax only in respect of the share of profits actually granted to them, and their position, in regard to income taxes, is similar to that of a shareholder.)

A *limited partnership with share capital* is likewise not a legal entity. It is a partnership consisting of one or more jointly responsible members and of a number of sleeping or limited partners whose interest is transferable and who are merely bound by their stake in the partnership, this amount being represented by shares. The estate of such a partnership is separate from that of its shareholders or limited partners. The profits distributed to the latter are subject to the same fiscal treatment as the profits of share companies. That is to say, the tax on dividends is imposed on them when they are distributed and they are further subject to income tax in the hands of the shareholders.

The fiscal treatment of the income of managing partners of the above-mentioned limited partnerships with share capital is the same as that of the income of members of partnerships.

The pure form of capital association is the *share company*. Vested with a legal entity, it has an existence of its own, and the liability of its shareholders is limited to their share in the company's capital. It also affords them certain fiscal advantages — *i.e.*, undistributed profits are liable neither to the tax on dividends and *tantièmes* nor to income taxes.

The tax on dividends and *tantièmes* applies also to *co-operative societies* (all of which have a legal entity), to *all other profit-seeking associations*, whether invested with a legal entity or not, and to

¹ "Wet op de Dividend- en Tantiëmebelasting 1917" (Law of January 4th, 1918, *Staatsblad*, No. 4).

² Supreme Court, December 31st, 1924, B., No. 3559, Vol. XII, page 588.

mutual insurance companies (which are legal entities). The scope of the present survey precludes dealing with these companies and associations, which, moreover, rarely extend their business activities beyond the national frontiers.

The above-mentioned tax is further applicable to share companies which, though incorporated in a foreign country, are in fact domiciled in the Netherlands.¹

In determining the State in which a company has its *de facto domicile*, little importance is attached to the centre of its operations.² The company is domiciled in the country where it has its *central seat of management*. If this seat is in the Netherlands, the company is regarded, for purposes of the present survey, as Dutch. On the other hand, the tax owing by such company is assessed and collected in the commune where the most important part of its Netherlands business is situated (Article 14 *bis* of the above-mentioned law). The place of assessment is of no importance in determining the amount of tax.

2. TAXABLE DISTRIBUTIONS AND SALARIES.

The tax is levied upon :

(a) Distributions³ of profits of a company to persons being entitled to a share of its total net profits (even if the amount distributed is a remuneration for services rendered to the company), subject to certain exemptions ;

(b) *Taxable salaries*⁴—*i.e.*, remuneration paid to managers or directors (*bestuurders* or *directeuren*), supervisors (*commissarissen*),⁵ and to other members of the governing body or of the staff of the company to the extent that they exceed, for each interested party and for a business year of twelve months, the amounts indicated below :

(1) 10,000 florins for managers or directors⁵ and other members of the company's staff ;

(2) For supervisors, a sum dependent on the statutory capital and which ranges from 200 florins (when the statutory capital does not exceed 500,000 florins) to 1,250 florins (when this capital amounts to or exceeds 3,500,000 florins).

By salaries, the law understands any remuneration which is not part of the company's total net profits, or, in other words, which is not to be considered as a "*tantième*" (within the meaning of the law). If a *share company* is entitled to this remuneration, it counts as a single person ; a partnership counts for as many persons as there are partners.

The persons enumerated in Article 2 of the Law, as well as the individuals or legal entities which are in a similar relation towards a company, are regarded as having a legal right to all the profits they receive from the company. Article 2 includes founders, persons having transferred to

¹ Supreme Court, March 11th, 1926, B., No. 3788 (Vol. X, page 288) : the operative side of the business was conducted in Netherlands East India, the management being established in the Netherlands. See, too, Rotterdam Court, December 19th, 1912, B., No. 1124 (Vol. IV, page 33) : a limited company which had a registered office in Great Britain, but nothing more. To-day it is the boards of appeal for direct taxes, not the courts, which determine fiscal domicile for purposes of direct taxes and the tax on dividends and *tantièmes*.

² Board of Appeal for Direct Taxes, No. I, Amsterdam, March 7th, 1922, B., No. 2991 (Vol. VIII, page 339). The appeal against this judgment was dismissed (B., No. 2991, note).

³ Articles 2, 4, 5, 6, 8 and 9 *bis* of the Law.

⁴ Article 7 of the Law.

⁵ The structure of Dutch companies does not exactly coincide with that of French or Anglo-Saxon companies. For example, the directors are managers belonging to the staff of the company. (In so far as companies organised under French or Belgian law, or companies organised in the Netherlands after the plan of French or Belgian companies, are concerned, and if these companies have their *de facto domicile* in the Netherlands, the managing directors (*administrateurs délégués*) are assimilated to "*bestuurders*" or "*directeuren*" (managers) and the other members of the board of directors (*conseil d'administration*) as well as the auditors (*commissaires aux comptes*) to the "*commissarissen*" of the Dutch law.)

the company the exploitation of a concession held by them, shareholders of all kinds, members (of a co-operative society or other association), participants (in a mutual insurance company), holders of shares in a guarantee fund (of such companies), supervisors and managing directors. If a company distributes profits to other categories of persons, these distributions are taxable only to the extent that such persons were entitled to claim these sums.¹

The fact that a distribution is made in consideration of services rendered or goods supplied to the company does not prevent its being taxable.² Thus all the advantages stipulated as consideration for the use of a concession, patent, copyright or real estate and loans of money as well as personal services are taxable if they are dependent upon the net profits of the whole company.

Exemptions.

The following are not liable to the tax :

- (a) Distributions to the State under a provision of public law (Article 4 (a)) ;
- (b) Distributions to the shareholders of public utility share companies, provided that all the shareholders are public corporations (Article 4 (b)) ;
- (c) The profits accruing to jointly and severally liable partners of limited partnerships with share capital (Article 4 (c)) ;
- (d) Distributions made to shareholders after a company has reduced, by reason of losses, the face value of the shares. This exemption, however, is limited to the amount of such deductions made prior to the distributions concerned (Article 5, paragraph 3 (a)) ;
- (e) Any distribution to the members or shareholders of an association or company, if proportionate to goods or services supplied by the recipient of such distributions (Article 5, paragraph 3 (b)) ;
- (f) The amount of *tantièmes* paid to a managing director or to any other member of the staff, in so far as his salary is less than 10,000 florins (Article 8 ; and for *salaries*, see Article 7, page 335) ;
- (g) Salaries and *tantièmes* paid to persons in the company's services who are obliged to exercise their functions outside the Netherlands (Article 9 *bis*).

3. ASSESSMENT OF TAX.

(a) *Computation of Taxable Amount and Deductions.*

For purposes of applying the law on the tax on dividends and *tantièmes*, every distribution of profits is held to refer to a business year. In most cases there is no doubt as to the year to which the distribution refers, even in the case of interim dividends. Surpluses distributed when a company is wound up are regarded as referring to one or more years, according to circumstances.

Distributions which are made not corresponding to an excess of net assets of the company towards the capital paid up by the shareholders are considered as distributions relating to the following business years in the course of which profits will serve to reconstruct the company's estate up to the amount of capital paid up (Article 5, paragraph 2). If a company refunds to its shareholders part of the paid-up capital instead of distributing its profits, although its net assets exceed that capital, a dividend is considered to have been distributed to the extent that the profits of the company cover the refund of capital. This provision does not apply if the company can prove that sound commercial practice required a repayment of the capital (Article 5, paragraph 1 (b)).

¹ See Judgments of the Supreme Court of May 30th, 1923, B., No. 3252 (Vol. IX, page 109), and of June 1st, 1921, B., No. 2831 (Vol. VIII, page 45).

² Supreme Court, September 26th, 1923, B., No. 3290 (Vol. IX, page 172).

If a company, etc., increases its paid-up capital by a free issue of shares or by increasing the nominally paid-up value of the existing shares, the operation is held to constitute a distribution of dividend followed by a payment of capital by the shareholders (Article 5, paragraph 1 (a)).¹

For the purposes of determining "paid-up" capital, account should be taken of the actual value of property brought into the company by the founders (this value being estimated at the time when the property is brought into the company), as well as the sums actually paid in cash by the shareholders into the hands of the company. When, however, a share company incorporated in the Netherlands issues shares below their face value to regular middlemen (Article 38 (a), paragraph 2, of the Netherlands Commercial Code), the company is deemed to receive the amount of the face value, the discount being considered as part of the cost of issue.

An *agio*, concealed or not, is therefore to be considered as part of the capital. If the company has made refunds of capital which have not been considered as dividends, these refunds diminish the paid-up capital; if, owing to loss, the company partially redeems its statutory capital by stamping the certificates, that operation likewise reduces the capital paid up, but at the same time secures potential exemption (see above).

Net assets and paid-up capital are computed on the basis of the situation at the end of the business year to which the distribution refers.

If the distribution is not in cash (*e.g.*, when goods are sold below their value), it is assessed from the point of view of the company. The same applies to salaries in kind (*e.g.*, free housing accommodation).

The law makes no rule for assessing a company's net assets. Doubtful cases are rare, since a company will hardly ever contend, when distributing dividends, that the excess of its net assets over paid-up capital is less than the amount distributed. The Supreme Court has upheld² the view of the administration that, for the computation of net assets, account must be taken of the company's goodwill and that the administration may assess that goodwill at its real value, if this is not equal to the book value.

Deductions for the Purpose of avoiding Internal Double Taxation.

Income which a share company enjoys in the course of the financial year by holding shares in another company or association, the distributions of which are in principle subject to tax, is deducted from the total distribution of profits liable to tax in the company's name, on condition that the shares were in the company's possession for the whole of the financial year in which the income was received. If the deduction allowable on this score exceeds the taxable distribution, the surplus is deducted from its subsequent distributions (Article 3).

Deductions for the Purpose of avoiding International Double Taxation.

Articles 29, 27 and 28 aim at diminishing to a certain degree the double taxation of Netherlands companies due to the fact that all or part of their profits consist of dividends of colonial or foreign companies (Article 29) or to the fact that their operations extend to the colonies (Article 27) or abroad (Article 28). Article 29 runs as follows:

"If a corporation, association or company whose distributions of profits are liable to tax holds shares in a corporation, association or company established³ in Netherlands East India, Surinam, Curaçao or abroad, and is there subject to a tax in favour of the central Government and if this tax is levied in any manner whatsoever in proportion to profits, two-thirds of the

¹ The same legal construction applies in connection with the registration fee paid once only for the capital subscribed and paid up.

² November 14th, 1928, B., No. 4393 (Vol. XI, page 661).

³ *i.e.*, having its fiscal domicile.

sum which the corporation, association or company has enjoyed from these shares in the course of a business year are deducted from the following distribution of profits before assessing tax, provided that it held these shares for the whole of the business year during which the sums previously mentioned were received."

If the deduction allowed exceeds the taxable distribution, it is carried forward to the next year ; deduction, therefore, is not barred by limitation, but must be made as soon as possible.

Articles 27 and 28 deal with quite a different form of deduction. We need only describe the principles of Article 28 concerning enterprises taxable abroad ; Article 27 contains similar rules for companies, etc., taxable in the colonies.

Article 28 lays down that two-thirds of the portion of distributed profits derived from activities abroad must be deducted from the amount of the taxable distribution. The law prescribes that the portion of the taxable distribution derived from abroad shall be determined by fractional apportionment. In the case of insurance enterprises, this apportionment must be based upon the ratio between premiums and capital received.¹ The basis of apportionment for all other enterprises is the business result for the fiscal year concerned, computed in accordance with Articles 7, 10 and 11 of the Income Tax Law.²

In order that companies may benefit by the provisions of Articles 27 and 28, the income must have been taxable in the name of the company in one form or another, abroad or in the colonies.

(b) *Computation of Tax.*

These deductions, it should be pointed out, apply to taxable distributions, but never to salaries subject to tax. Thus it may happen that, owing to the deductions allowed, distributions are not taxable, while salaries remain liable. The rate of tax is 5 per cent plus 33 "additional cents" for the loan fund and 48 "additional cents" for the commune or communes concerned — that is to say, 9.05 per cent in all.

There are no deductions from the tax.

4. COLLECTION OF TAX.

No profits may be distributed until the directors of the company have declared them to the office of the competent inspector of direct taxes. The return must also include all salaries taxable in part (Articles 12 and 13).

A negative return is required in the following cases :

If it has been decided to make no distribution (the return to be made within a fortnight of such decision) ;

If, with reference to a given business year and without any formal decision being necessary, no distribution is made (the return to be made within three months from the end of the business year) ;

Or if, at the end of a year after the conclusion of the financial period, the required decision has not yet been taken to make or not to make a distribution of profits for that period (the return to be made within a fortnight from the end of the year).

In the last-mentioned case the negative return must be repeated each year until finally decision is taken.

Salaries partly taxable must be included in the negative returns unless they have already been declared in a previous negative return for the same business year (Article 12).

¹ See page 371.

² See pages 343 and 344.

A certified true copy of balance-sheets and profit-and-loss accounts or of the documents replacing them must be forwarded to the inspector of taxes within a fortnight of the approval of the balance-sheet or of the documents replacing them (Article 14).

In the absence of a return, the fiscal administration may assess tax *ex officio*, and if a return is made, it may disregard the information contained therein if it seems inexact. In the latter event, the inspector responsible for assessment must make his objections known to the managing directors of the company in question and give them reasonable time to reply thereto (Article 16). Before the tax is fixed, the directors must, at the inspector's request, consent to an examination of the company's books and of the documents in support of their return or statements (Article 17). When the tax is fixed, a notice is sent to the company (Article 18).

Within two months of the assessment notice, the directors may file an appeal with explanations against the amount of tax to the local Board of Appeal for Direct Taxes (Article 19). Appeal against the board's decision lies with the Supreme Court (Hooge Raad der Nederlanden).¹

The tax is payable within fourteen days of receiving the assessment notice (Article 38).

Pending a final assessment, a provisional figure may be entered on the assessment list in conformity with the return. In special cases a supplementary amended assessment may be made after the so-called final assessment.

III. TAXES ON INCOME.

The Netherlands have two taxes on income : the *income tax proper* (*inkomstenbelasting*)² and the *tax on behalf of the Communal Fund* (*Gemeentefondsbelasting*).³ These two taxes are closely connected ; the taxable income is determined in the same way for each and their assessment is simultaneous.

I. TAXPAYERS.

Income tax is levied in the first place upon *individuals* who have their fiscal domicile in the Netherlands (Income Tax Law, Article 1). As we shall see later, these persons are liable in respect of both national and foreign income, but, in order to avoid double taxation, the tax is in some cases reduced if the total income includes foreign income.

The tax is further imposed upon foundations which have their fiscal domicile in the Netherlands and engage in profit-seeking activities there or elsewhere (Income Tax Law, Article 1). In their case there is no provision for the avoidance of double taxation.

Lastly, all individuals and legal entities who have no fiscal domicile in the Netherlands, but enjoy income from Netherlands sources, are liable to income tax. Article 2 of the Law enumerates these persons, and the list corresponds more or less to the income enumerated in Article 24 (see below). There are, however, cases in which personal liability to tax does not quite coincide with income as enumerated in that article, and in these cases tax is not levied.

Individuals and legal entities liable to income tax are also liable to tax on behalf of the Communal Fund, except foundations having their fiscal domicile in the Netherlands and individuals or legal entities domiciled for fiscal purposes in overseas territories (Article 12 of the Law of 1929, *Staatsblad*, No. 388). On the other hand, an inhabitant of the Netherlands in receipt of colonial income does not thereby obtain any reduction of the tax on behalf of the communes (Article 14 of the same law), nor does he obtain such reduction if he derives income from abroad.

¹ Articles 18 *et seq.* of Law of December 19th, 1914 (*Staatsblad*, No. 564), concerning Boards of Appeal for Direct Taxes.

² Law of December 19th, 1914 (*Staatsblad*, No. 563), concerning income tax.

³ Law of July 15th, 1929 (*Staatsblad*, No. 388), concerning the revision of the financial relations between the State and the communes.

The *fiscal domicile* of individuals is in the country where they are *de facto* domiciled. (For the domicile of other taxpayers, see page 335.) Thus the law prescribes that the question whether a person is permanently resident in the Kingdom shall depend upon circumstances (Income Tax Law, Article 1, and Property Tax Law, Article 1). The law on income (and property) tax recognises no such legal domicile as that of a woman living at her husband's domicile or that of a minor at his parent's or guardian's domicile. Nearly all persons who live in the Netherlands have a fixed abode in the Kingdom, but there is a class of itinerant persons who inhabit the Kingdom without having any fixed abode in a particular commune.¹

The law does not specify the circumstances that determine fiscal domicile; the rule is that all relevant circumstances shall be taken into account. Not all these, of course, are of the same importance.

It would be quite contrary to the spirit and intention of the law to give a definition of fiscal domicile, as the legislator did not want such a definition to be given. It could only be said that a person is domiciled in the place where he is presumed constantly to be.² Practice inclines to give the most weight to the following:³

- (a) The place in which is situated the house where the person concerned most frequently passes the night;
- (b) The place where his activities (profit-seeking and other) and recreation are centred;
- (c) The place in which the family or household to which he belongs most frequently passes the night.

In the event of discrepancy and if the particulars concerning two of the places mentioned above coincide, those two take precedence of the third. Otherwise (a) takes precedence of (b) or (c), and (b) takes precedence of (c).

One authority,⁴ however, is of opinion that (c) is the most important consideration and should take precedence of (a) and (b) together. If a person has temporarily left the country, the important point to consider is what evidence he showed of an intention to return shortly (say within fifteen months). Moreover, a person may quite possibly have ceased to inhabit the Netherlands without intending ever to return there⁵ or to settle elsewhere.⁶ According to the Supreme Court,⁷ a person may live in several countries at the same time, but this jurisprudence ruling does not in fact entail double taxation.

It is quite a mistake to suppose, as some do, that a person acquires fiscal domicile in the Netherlands by three months' residence there. There is no such fixed period and, generally speaking, no fiscal obligation rests on a person who stays in the Netherlands for three months without any obvious intention of settling in the country.

If a person re-establishes himself in the Netherlands in the course of the year beginning on the date when he has ceased to have there his fiscal domicile, the law considers that his return has

¹ Supreme Court, June 25th, 1930, B., No. 4766 (Vol. XII, page 567). See also Income Tax Law, Article 53: persons living in the country without being resident in any particular commune are assessed for tax wherever they may be traced or found.

² Supreme Court, November 2nd, 1927, B., No. 4144 (Vol. XI, page 272).

³ As a consequence of the division of the jurisdiction between the Courts, there exist precedents of the Supreme Court and Boards of Appeal for Direct Taxes (on the question whether a person resides — or still resides — in the Kingdom) and of the Crown assisted by the Claims Department of the State Council (as to what commune tax shall be assessed in). See Articles 54, 77 and 98 of the Income Tax Law and Articles 12, 27 and 30 of the Property Tax Law.

⁴ Dr. J. H. R. Sinninghe Damsté, Director-General of Taxes, in his book "De wet op de Inkomstenbelasting", 4th edition, page 53; pages 52-61 contain a collection of jurisprudence on the fiscal domicile of individuals.

⁵ Supreme Court, April 29th, 1925, B., No. 3601 (Vol. X, page 3).

⁶ Supreme Court, October 8th, 1924, B., No. 3526 (Vol. IX, page 512).

⁷ Supreme Court, March 23rd, 1927, B., No. 4038 (Vol. XI, page 85).

taken place at the same date as his departure, unless it is clear that he has had in the meanwhile his fiscal domicile in the territory of a foreign country (Income Tax Law, Article 1, paragraph 2). Persons who sojourn in the Netherlands temporarily while they have, or are deemed still to have, in accordance with the Income or Property Tax Laws of the territory in question, their domicile in one of the overseas territories (Income Tax Law, Article 1, paragraph 3) are considered as having no domicile in the Kingdom.

2. TAXABLE INCOME.

(a) *Income of Individuals domiciled in the Netherlands.*

Individuals who have their fiscal domicile in the Netherlands are liable in respect of their *net income*. Net income within the meaning of the law is gross income (*i.e.*, the total net yield from all sources of income situated in the country or elsewhere) less certain personal deductions cited in the Income Tax Law, Article 19. These personal deductions have no relation to any special source of income.

The law distinguishes four classes of sources of income (Income Tax Law, Article 4) — *viz.* :

- Real property ;
- Movable capital ;
- Industry and labour ;
- Rights to life annuities and pensions.

Income from real property is the profits derived — apart from the carrying-on of a business or profession — from buildings and lands, including the rental value of premises which the taxpayer devotes to his personal use (Income Tax Law, Article 5).

Income from movable capital is the yield of capital which is not in the form of real property and which the taxpayer does not use for the carrying-on of his business, such as dividends and interest on securities and, *inter alia*, the payments accruing to limited partners, interest on all debts whether or not based on a legal instrument or secured on mortgage.

Shares and bonds issued to shareholders without a payment on their part corresponding to the entire face value are regarded as dividends. The amount of these dividends is estimated to be equal to the amount for which payment is not shown. The same is true in connection with the increase in the nominally paid-up value of shares for which the parties concerned have made no equivalent payment.

A total or partial refund of the sum paid for shares to a company is regarded as a dividend distribution, to the extent that there is a net profit — unless the company's capital has previously been reduced by an amendment of its statutes (Income Tax Law, Article 6).

As a rule, the Supreme Court regards as movable capital all tangible and intangible personal property, the income from which is not mentioned in Articles 7 and 8 concerning income from industry and labour and rights to life annuities and pensions.

Income from industry and labour comprises all profits not regarded as income from movable capital and derived from enterprises, professions (liberal or salaried) and from operations, activities and services of all kinds (Income Tax Law, Article 7), except gain from pure speculation unconnected with the carrying-on of business (Article 9 (*d*)) and profits from forestry (except the cutting of underwood) (Article 9 (*e*)).

Income from life annuities and pensions includes payments of furlough allowances, public and private pensions, annuities, alimony and family allowances, in cash and in kind, provided they are due under the law, and generally all payments and advantages not connected with the discharge of some function or employment, and which, moreover, finish with the life of the beneficiary or a third party (Income Tax Law, Article 8).

Maintenance and education allowances received by minors from their parents, as well as pensions and life annuities granted to them by the latter, are not subject to tax (Article 9 (a)).

(b) *Income of Foundations established in the Netherlands.*

Foundations which have their fiscal domicile in the Netherlands are liable in respect of the net yield of their profit-earning activities, unless these activities, although profit-earning, have a more or less charitable character (Income Tax Law, Article 23).

(c) *Income of Individuals and Legal Entities not domiciled in the Netherlands.*

The law distinguishes two classes of taxpayer whose fiscal domicile is not in the Netherlands. The first may be called that of foreign individuals (including partners in ordinary partnership), and the second that of foreign legal entities (associations whose profits accrue direct to the members are not in this class).¹

Apart from the tax scale, the distinction is of no great importance, for Article 26 of the Income Tax Law prescribes that the taxable income of foreign legal entities shall be computed in the same way as that of foreign individuals. The latter, under Article 24, is computed like the net or taxable income of individuals domiciled in the Netherlands, except that account is taken only of income derived from the sources enumerated below :

1. Real property situated in the Netherlands (for income from real property) ;
2. Loans secured on real property situated in the Netherlands ; and all other sources except securities, to the extent that the yield from these sources is composed by a part of the net yield of business activities having their seat (*i.e.*, centre) in the Kingdom (for income from movable capital) ;
3. Business and professional activities in so far as they are carried on within the Kingdom and functions remunerated by a Netherlands public fund in so far as they are fulfilled outside the Kingdom (for income from industry and labour) ;
4. Rights to furlough allowances or pensions paid by the civil pensions fund or the funds of a Netherlands public corporation (for pensions and annuities).

Accordingly, the law does not define Netherlands *income*, but it defines Netherlands *sources* of income, which it divides into the four main classes cited in Article 4. Consequently, in order to determine whether income is taxable in the Netherlands, one must first ascertain its sources.²

The fiscal regime described above does not apply to foreign railways and tramways with regard to their lines going beyond the Netherlands frontier, or to foreign insurance companies, or to the carrying-on of business or professional activities in the Kingdom purely temporarily (Income Tax Law, Article 27). For these enterprises and activities there exist special provisions.

Under Article 30, individuals and legal entities who personally or through a representative carry on a business or profession in the Netherlands temporarily, but for at least three consecutive months, are liable in respect of the whole net profit earned in the Netherlands. When it speaks of "whole net yield", the law means that there shall be no deduction of the share of profits accruing to any participant. That is also why none of the participants is mentioned in Article 2 as being personally liable.

¹ See page 334.

² For details, see pages 356-359 below.

3. ASSESSMENT OF TAX.

(a) *Computation of Taxable Income. Deductions and Increments.**Individuals domiciled in the Netherlands.*

A very important concept for the purposes of the computation of income is that of *source of income*. Each property, claim, security, enterprise, independent profession, employment, etc., capable of yielding income to the taxpayer is regarded as a separate source for him, subject to the restriction that real and personal property which is connected with the carrying-on of business is not considered as a source of income distinct from the business. Article 15 provides that, in principle, promotion and transfers within a public administration or in the service of a private person or organisation shall not be regarded as creating a fresh source of income. On the other hand, paragraph 2 of the same article says that a new source is created when a person takes up a post within the Kingdom after having fulfilled functions either abroad or in oversea territories.

The income of a married woman and her liabilities in respect of which personal deductions are granted (Article 19) are regarded as the income and liabilities of her husband (Income Tax Law, Article 31). This is not the case when she is separated from the bed and board of her husband, or if there is only a judicial separation of estates, and, apart from these cases, so far as she has reserved for herself the entire or partial management of her property and enjoyment of her income (Article 32, paragraph 1).

For the purposes of assessment, the net yield of the various sources of income is added and — as far as possible — deduction is made of losses (Article 17, paragraph 1) incurred in respect of all sources of income existing at the beginning of the tax year (Article 12) — *i.e.*, on May 1st¹ (Article 40).

The profit-making activities which the taxpayer (or his wife) carried on before that date are deemed to be sources of income existing at that time, unless they have been definitely given up.

In order to determine the net income for the year from each source — *i.e.*,² the net income which the taxpayer will enjoy during the current tax year — the law employs two different methods. The first applies to *sources of income already in existence* throughout the whole of the preceding calendar year (or, in the case of business income, throughout a whole business period, supposing that the latter does not coincide with the calendar year). The net annual income from these sources is assessed, according to Article 13, at the net yield for the previous calendar or business year, except that dividends, *tantièmes* and other shares in the yield³ of a business which the taxpayer does not himself conduct are regarded as income belonging to the calendar year in which its amount was determined.

As regards *fresh sources of income*, Article 14 prescribes another method. The net annual yield (*i.e.*, the yield for the tax year⁴ from these sources is estimated on the basis of the facts existing at the beginning of the tax year in question. No special provision applies in this case to dividends and *tantièmes*; consequently, dividends are computed at the amount which will be payable during the tax year; *tantièmes*, at the amount of the remuneration corresponding to the functions which the party concerned will accomplish during that same year. The shares of limited partners are treated in the same manner as *tantièmes*.

Funds temporarily uninvested are regarded as a source of income and are ascribed a presumed yield. This is determined according to the intended investment or, if no investment has yet been decided upon, the yield is fixed at 4 per cent (Article 16).

¹ In the case of persons whose personal liability to tax starts in the course of the tax year (birth, new establishment, etc.), tax is assessed on the basis of the situation as it exists at the time when fiscal liability arises (Articles 12 and 14). This principle applies also to deductions in so far as these are dependent upon the position at the beginning of the fiscal year (Articles 19 and 38).

² Supreme Court, April 30th, 1924, B., No. 3404 (Vol. IX, page 357).

³ That is to say, *net yield*; Supreme Court, May 4th, 1927, *Bestellingen in Belastingzaken*, No. 4056 (Vol. XI, page 121).

⁴ See *Bestellingen in Belastingzaken*, No. 3402.

Special provision is made in Article 18 for income from isolated operations, activities or services, as, for instance, the activity of a person who makes an invention or writes a book without regularly devoting himself to such occupation. The net profit or loss which such operations, activities or services have brought or yielded to the taxpayer during the previous calendar year are added to (or deducted from) net income from more permanent sources.

Deductions.

The deductions which may have to be made in the course of the computation of the taxable amount may be grouped into four classes :

Impersonal deductions made from the gross yield from each source of income separately, in order to obtain the net yield from each source (Articles 10 and 11) ;

Losses brought forward from previous tax years (Article 17, paragraph 2) ; this deduction is made from the total net yield of the sources not included in Article 18 (concerning isolated operations, activities and services) *before* applying that article ;

Personal deductions from "gross income" — *i.e.*, from the net amount obtained after adding together the net yield of the various sources, taking into account the losses, and after having subsequently subtracted the losses carried forward and finally adding or subtracting the results of isolated operations ; these personal deductions are prescribed in Article 19 and give the net or taxable income ;

The deduction for children, provided for in Article 38 ; this deduction applied to net or taxable income gives the actual taxable amount.

1. *Impersonal Deductions.* — To obtain the net yield of each source of income, there is deducted from its gross yield the *cost* of acquiring, collecting and maintaining the yield, as well as the *charges* thereto related. The charges, of which Article 10 gives an illustrative enumeration, include business and professional expenses. These are defined as the expenses necessarily or directly related to the carrying-on of a business or profession and include costs of upkeep.

The following are, however, not considered as business expenses : expenses incurred for the purchase, erection, improvement or alteration of buildings, machinery, tools and other property destined for the carrying-on of a business or professional activity, the expenses of the purchase, extension or modification of an enterprise and other similar expenses (Article 11). This exclusion does not apply to: (1) expenses necessary for the replacement of property, the amortisation of which is not customary or compulsory ; (2) expenses for acquiring articles of small value, in so far as they may be considered as current expenditure.

The same Article 11 formally prohibits the deduction of sums destined for the creation or increase of reserve funds and interest on the taxpayer's capital.

In addition to business expenses, deduction should be made of the amounts set aside for depreciation and depletion of property employed in the business, as well as for bad or doubtful debts, these items being computed or estimated in accordance with sound business practice (Article 10, paragraph 2). As regards non-business sources of income, deduction is made of the depreciation which would be necessary in view of the expiry of rights at a fixed date (Article 10, paragraph 3). The last paragraph of that article provides for a special deduction on account of salaries, other remuneration, furlough allowances and retired pay. Contributions due to special funds in favour of employees or their relatives are also deductible.

2. *Losses brought forward.* — If in one of the two preceding tax years the losses from one or more sources of income not coming within the scope of Article 18 (isolated activities) have exceeded the net yield relating to other normal sources of income, the excess loss is also deductible. If these losses refer to the last tax year but one, they are reduced by the amount which may have been deducted for the preceding year. For each tax year the deductible amount of losses brought forward is computed *before* applying Article 18 (isolated operations, etc.). Thus a person may be taxed on the profits from isolated transactions, even when he has suffered a net loss on income from permanent

sources — a loss which he may apportion and deduct from his income from permanent sources in the following years.

3. *Personal Deductions.* — The personal deductions of Article 19 are the result of liabilities that do not relate to any specific source of income. The law gives the following exclusive enumeration :

Annuities, pensions and other periodical payments and advantages referred to in Article 8, with the exception of maintenance and education expenses of minors and annuities and pensions allowed to the taxpayer's minor children or those of his wife ;

Funded annuities ;

Interest charges ;

Life-insurance, annuity or pension premiums.

The annual amount of these liabilities, computed according to the situation at the beginning of the tax year, is deductible, but in the case of premiums the deduction is limited to 100 florins or, if the income is below 2,000 florins, to 5 per cent of the income.

4. *Deduction for Children.* — In the case of income tax proper, the taxable amount is obtained by taking from the net or taxable income the deduction in respect of children referred to in Article 38 of the Income Tax Law (see Annex). If a married woman has an income separate from that of her husband and if both husband and wife have their fiscal domicile in the Netherlands, this deduction is applied to the whole of the combined net income of husband and wife (Article 32, last paragraph) ; this provision does not apply in the case of separation from bed and board. A similar deduction as for the income tax proper is allowed for the Communal Fund Tax.

The deduction for children is granted in respect of the taxpayer's children, the children of the other party to the marriage and other children whom they maintain and bring up as their own, on condition, however, that these children are not themselves liable to the same tax (income tax or tax on behalf of the Communal Fund, according to which of the two is being assessed).

5. *Increments.* — As regards, more particularly, *the tax on behalf of the Communal Fund*, the net income, diminished by the deduction for children, is increased :

By 100 florins if the taxpayer is unmarried, but not if he has already been married and benefits by the deduction for children ;

By 100 florins if the taxpayer has his fiscal domicile in a commune classed in the second category, ¹ or if, though resident in the Netherlands, he does not reside in any specific commune ;

By 200 florins if the fiscal domicile is in a commune in the third category ; ¹

By 50 florins for each member of the taxpayer's family (including the taxpayer himself) who lives in the same household as he and is liable to the same tax, subject to the fact that a married couple always counts as one person and the increase in question does not apply to persons who, except for such increase, would not be assessed. ²

Foundations established in the Netherlands.

Foundations are taxable in respect of the profits they derive from business activities they are engaged in at the beginning of the tax year. The net profits for the year are estimated at the amount that these activities yielded in the previous business year. It is computed in accordance with the principles of Articles 7, 10 and 11. The only deductions permitted are the impersonal deductions referred to in Articles 10 and 11. ³ *Tantièmes* and shares in the profits by members of the staff are deductible in virtue of Article 10.

¹ For classification of communes, see Article 14 of the Law of July 15th, 1929 (*Staatsblad*, No. 388).

² See Article 14 of Law of July 15th, 1929 (*Staatsblad*, No. 388).

³ See page 344

Individuals and Legal Entities not domiciled in the Netherlands.

The taxable income of taxpayers not domiciled for fiscal purposes in the Netherlands is as a rule determined in the same way as that of individuals domiciled in the country. In view of the fact that, in the case of taxpayers domiciled abroad, only the sources of income enumerated on page 342 need be taken into account, the provisions concerning funds temporarily unemployed (Article 16) and isolated activities (Article 18) do not apply.

A special method of computation is applied to foreign taxpayers who (a) operate a railway or tram-line crossing the frontier (Article 28); (b) conduct an insurance enterprise (Article 29); (c) engage in temporary business or professional activities in the Netherlands (Article 30). In the case of (a) and (b), if the personal tax liability still exists at the beginning of the tax year, tax is computed on the basis of the Netherlands profits of the previous business year (for details, see page 343); as regards the business activities referred to in Article 30 (case (c)), the tax is levied on the profits actually earned during the current tax year.¹

The law lays down that tax shall be computed separately for each category of business activities referred to in (a), (b) and (c). In the unlikely event of a foreign company simultaneously operating in the Netherlands a factory, an international railway, an insurance enterprise and a travelling circus, the company would be considered as four different taxpayers.

1. *Impersonal Deductions.* — These are the same as for taxpayers domiciled in the Netherlands. The law, be it noted, does not regard interest on mortgage debts as a direct charge on the income from real property (see below under "Personal Deductions"). Further, Article 26 prescribes that, in the case of foreign legal entities, the taxable amount is computed as for individuals not domiciled in the Netherlands. Accordingly, percentages paid to the staff of a share company domiciled abroad are in principle deductible,² as are also other shares in profits accruing in one form or another to third parties other than holders of shares of stock, bonus and founders' shares, whether such participations in the profits are taxable in the hands of the beneficiary³ or not.

Percentages of any kind paid by foreign share companies are thus treated more favourably than those of Netherlands companies, since the latter are liable to the tax on dividends and *tantièmes* before being taxed in the Netherlands or elsewhere in the hands of the recipient.

The companies referred to in Article 30, however — *i.e.*, those which temporarily carry on business in the Netherlands — are not allowed to deduct the percentages and shares in the profits they distribute.

2. *Losses brought forward.* — It is considered that losses may no longer be carried forward when the taxpayer transfers his domicile from the Netherlands to abroad or *vice versa*.

3. *Personal Deductions.* — These are limited to the interest on mortgage debts situated in the Netherlands.

4. *Deduction for Children.* — This deduction is not allowed to taxpayers who are not domiciled in the Netherlands. In their case, therefore, "net or taxable income" is identical with the "taxable amount".

5. *Increments.* — Increases, in regard to the tax on behalf of the Communal Fund, do not apply to taxpayers not domiciled in the Netherlands.

¹ After these activities have been carried on for three months and, in subsequent years, at the beginning of the tax year, the yield of the whole tax year is estimated and the tax is fixed on the basis thereof. The authorities may reassess at the end of each quarter and establish a higher figure in an additional assessment (Article 42); on the conclusion of the taxpayer's operations in the Netherlands or at the end of the tax year, a final figure is fixed or any excess tax paid is refunded to the taxpayer on application.

² See judgments of the Supreme Court dated December 11th, 1918, B., No. 2112 (Vol. VI, page 139), and June 12th, 1929, B., No. 4526 (Vol. XII, page 180).

³ On the ground, for example, that the percentage is to be regarded as part of the profits of a profession carried on in the Netherlands.

(b) Computation of Tax and Deductions.

If a married woman not separated from the bed and board of her husband has an income separate from the latter's, and if both have their fiscal domicile in the Netherlands, the tax is computed on their combined net income (less the deduction for children, and, as regards to the tax on behalf of the Communal Fund, plus the increment for the purpose of that tax) and then allocated in proportion to the separate net incomes of husband and wife (Article 32, last paragraph).

The amount of income tax payable by individuals is obtained by applying to the taxable amount the sliding scale in Article 37 of the Income Tax Law ;¹ their tax on behalf of the Communal Fund is in accordance with the sliding scale of Article 15 of the 1929 Law.¹ The special rate applying to persons living in the parts classed in the first category of the communes of Amsterdam, Rotterdam and The Hague does not apply to taxpayers whose fiscal domicile is outside the Kingdom.

In the case of individuals, the income tax amounts to 6.40 florins per 100 florins of taxable income (Income Tax Law, Article 39) ; the tax on behalf of the Communal Fund is 2 florins per 100 (1929 Law, Article 17).

The income tax proper is subject to an additional tax of 20 cents for the loan fund and to the other additional cents shown in the Annex (Table of Tariffs). The latter additional cents are not imposed upon foreigners, who are likewise exempt from payment of the additional cents on behalf of the communes levied as a supplement to the tax on behalf of the Communal Fund.

Taxpayers whose personal tax liability arises in the course of the tax year are granted a reduction of tax amounting to one-twelfth for every whole month of the already expired tax year (Article 41).

*Deductions in order to avoid Double Taxation.**General Principles.*

The Netherlands being the third colonial Power in the world, Netherlands law has been concerned with problems of double taxation ever since the first income tax was introduced in 1893. As regards the two taxes on income, the provisions for the avoidance of double taxation granting a tax deduction only concern the income tax proper and individuals.

This deduction equals in principle the tax which the taxpayer would have to pay if his net income were equal to that which he derives from a given colony or foreign country. The deduction is thus computed per colony or country of origin as if the colony or foreign country determined net income in the same way and granted the same deduction for children and prescribed the same scale of tax as the Netherlands. The deduction is therefore independent of the tax scale and method of computation applied in the foreign country or the colony.

The deduction is not a deduction in favour of foreign income, but simply serves to avoid double taxation. Hence no deduction is ever allowed in respect of income which is not legally taxable in the colony or country of its origin. The fact, however, that income derived from a certain country is, on the grounds of its small amount; not taxed there does not prevent the granting of a deduction in the Netherlands. The same is the case when the colony or foreign country has accidentally omitted to impose tax.

Deductions on account of Colonial Taxes.

Vis-à-vis the colonies, the law has not seen fit to limit deduction to income from specific sources or to prescribe that income taxable in the colonies shall be reduced by the interest on mortgage

¹ See Annex.

debts situated therein. The deduction in question is dealt with by Article 99 of the Income Tax Law, which makes, in paragraph 2, an exception by prescribing special treatment for certain income. This article says :

“ If a person who has his fiscal domicile in the Netherlands is also liable to tax in Netherlands Indies, Surinam or Curaçao, the amount of tax, computed according to Articles 37 and 38, is diminished by the tax similarly computed, corresponding to net income equal to the part of his net income taxable in Netherlands Indies, Surinam or Curaçao.

“ The provision in paragraph 1 is not applicable to net yield from business or a profession carried on in a merely temporary manner in Netherlands Indies, Surinam or Curaçao. The Minister of Finance may take measures to avoid double taxation in this connection (—).”¹

Hitherto the Minister has issued only one measure in exercise of the powers thus conferred on him. That provision covers cases in which the following conditions are met with :

1. The activities constituting the source of income, which has been taxable in one of the oversea territories, must still be exercised at the beginning of the tax year in question and the source of income must have existed for the taxpayer during one whole calendar or accounting year ;

2. During that year he must have exercised these same activities temporarily in overseas territories and have been subject to tax in respect thereof.

In the case, however, of an official or employee, his functions must be held to be discharged in the Netherlands at the same time as in the colonies, for otherwise, when the taxpayer is returned to the home country, a fresh source of income would be created (see Article 15 of the Income Tax Law) and the first condition would be unfulfilled.

If the ministerial ruling² is applicable, the relation is determined between : (a) income derived from these activities during the time when they were exercised in the colonies, and (b) total net income from all sources without personal deductions being made. This ratio, applied to the total tax, gives the amount to be deducted.

Deductions on account of Foreign Taxes.

The deductions to be made by reason of taxation in a foreign country are regulated by a decision of the Minister of Finance of April 17th, 1928 (*Staatscourant*, No. 76), which is now supported by Article 3³ of the Law of June 14th, 1930 (*Staatsblad*, No. 244). It is applicable to persons having their fiscal domicile in the Netherlands and have been there domiciled for the past five tax years, and to all other inhabitants of the Netherlands who are of Dutch nationality or are nationals of a foreign country which avoids, under conditions similar to those of the ministerial ruling, double taxation of Dutch nationals inhabiting its territory.⁴

In order that this deduction may be granted, the person concerned must be liable abroad to an income or property tax by reason of :

- The ownership or enjoyment of real property situated in the foreign country ;
- The possession or the enjoyment of the yield in his favour of a debt guaranteed by a mortgage on real estate situated in the foreign country ;
- The carrying-on of business in the foreign country ;

¹ The last sentence in paragraph 2 is omitted as being purely formal.

² Decision of the Minister of Finance, dated July 5th, 1928, No. 163 (*Staatscourant*, No. 130).

³ This article empowers the Finance Minister to take all necessary steps to avoid, in the case of individuals living in the Netherlands, the double taxation of income derived from sources taxable abroad.

⁴ e.g., Austria, Canada, United States of America and Union of South Africa.

The discharge of duties remunerated by a foreign public body ;
The enjoyment of a pension or furlough allowance granted in consideration of past services which were paid for by a foreign public body.

The deductible amount is obtained by taking as a basis the net income which the taxpayer would be deemed to enjoy under Netherlands law if he had only the sources taxed abroad, less interest on non-business debts secured on real property situated in the country in question ; the deduction for children is then made at the rate corresponding to this net income and the scale is applied to the balance. The amount thus obtained is deducted from the tax as computed according to the ordinary rules.

If real property is situated partly within the Netherlands and partly in a foreign country, the foreign part, in virtue of the above-mentioned decision, is regarded as a separate property. If a business or profession is carried on partly in the Netherlands and partly abroad, the foreign part is again regarded as a separate business or profession.

4. COLLECTION OF TAXES ON INCOME. ¹

Returns. — The taxpayer or his legal representative has to furnish a declaration of his income to the inspector of taxes within twenty days of receiving from the authorities a form for the purpose.

These returns are usually checked by the inspector of direct taxes. This official may request additional information from the taxpayer who has made a return, but the latter is not bound to furnish such information. On the other hand, if the taxpayer is obliged to keep accounts, the inspector is entitled to demand the submission of the books and documents which may be of use for the checking of the return and the information given by the party concerned.

Taxpayers may appeal against their assessment to the inspector himself within two months of the date of the assessment notice. They may then appeal against the administration's decision within a month from the date on which the decision was forwarded from the administration, by an explanatory letter, to the local Board of Appeal for Direct Taxes. The board's decision may itself be set aside by the Supreme Court.

Claims, appeals, etc., do not afford grounds for suspending payment.

Payment. — Taxes are paid to the collector of direct taxes at his office or through the post, or by post-office or bank transfer. As regards persons not domiciled in the Netherlands or having no fixed domicile there, tax is payable as soon as assessed. In other cases it is paid in monthly instalments. ²

IV. TAXES ON PROPERTY.

As already mentioned, there are two taxes on property, the *property tax* proper ³ and the *defence tax No. I*. ⁴ The receipts from the latter tax are paid into the Loan Fund. The two property taxes are still more closely connected than the two income taxes, since the same amounts form the basis of assessment for both property taxes. ⁵ They are assessed at the same time as income taxes.

¹ There is no withholding at source.

² See Land and Buildings Tax.

³ Legislation : Wet op de Vermogensbelasting 1892 (Law of September 27th, 1892, *Staatsblad*, No. 223, on the property tax).

⁴ Legislation : Wet van 16 Maart 1928 (*Staatsblad*, No. 66) tot herziening van de verdedigingsbelasting I (Law of March 16th, 1928, *Staatsblad*, No. 68, amending the defence tax No. I).

⁵ See Articles 1 and 2 of the Law of 1928.

I. TAXPAYERS.

Property taxes are levied on individuals whose fiscal domicile¹ is in the Netherlands (Property Tax Law, Article 1) and on individuals and legal entities whose fiscal domicile¹ is not in the Netherlands, but who :

Own or enjoy, in virtue of a property right, real estate situated in the Netherlands or a mortgage debt secured on such estate ;

Carry on in the Netherlands, either personally or through a representative, a business or independent profession (salaried employment does not come within the sphere of these taxes), unless only temporarily and for less than three consecutive months ;

Are entitled to a share in the profits in the net yield of a business carried on in the Netherlands (Property Tax Law, Article 2), unless on account of functions actually fulfilled or in the capacity of a holder of shares of stock or other negotiable shares.

2. TAXABLE PROPERTY.

Individuals domiciled in the Netherlands.

Tax is imposed upon the whole net property of a taxpayer domiciled in the Netherlands — *i.e.*, the total value of his property situated both in the Netherlands and abroad (gross property), less debts (Property Tax Law, Articles 3 and 8). In order, however, to avoid double taxation, the tax is in some cases reduced if the total property includes property taxed abroad.

The gross property includes all the taxpayer's assets recognised in law and having a cash value, including usufructs and current annuities (Property Tax Law, Article 3), except (Property Tax Law, Article 6) :

1. Articles of gold and silver, pearls and precious stones, of a value not exceeding 2,000 florins ; household furniture (within the meaning of Article 571 of the Netherlands Civil Code) ; *objets d'art* and scientific articles, food and clothing ; on condition, however, that these articles are not commercial stock or objects serving some professional or business purpose ;

2. Life-annuity and life-insurance policies, provided that these policies are not part of the assets of a business or profession. Moreover, as regards life-insurance policies, it is required that none of the premiums relating thereto (both initial and annual) shall exceed 8 per cent of the capital which will be due at the time of the decease of the person whose life is insured ;

3. Rights to current life annuities, the value of which does not exceed 1,200 florins a year, provided that they are in consideration for fixed premiums which have been paid for at least ten years and that the remainder of the net taxable property of the person concerned is less than 16,000 florins ;

4. Rights to retiring, invalidity, old-age and survivors' pensions paid either under the law or as a reward for past services ;

5. The legal usufruct of parents on the property of their children not of age and allowances due in virtue of the provisions of the civil law governing family relations ;

6. Periodical income of all kinds in so far as future instalments not yet due are concerned, as well as the ungathered produce of crops harvested at least every three years ;

7. Rights to annuities or other periodical payments granted by parents to their children under age.

¹ For fiscal domicile of individuals, see page 340, and for that of legal entities, page 335.

Individuals and Legal Entities not having their Fiscal Domicile in the Netherlands.

Under Article 9 *bis*, individuals and other taxpayers whose fiscal domicile is not in the Netherlands are liable in respect of their net property within the Kingdom — *i.e.*, the Netherlands portion of their gross property less certain debts. The possessions making up gross Netherlands property are the following (Article 9 *bis*):

1. Real estate situated in the Netherlands ;
2. Mortgage debts secured on real estate situated in the Netherlands ;
3. All other possessions situated in the Netherlands or elsewhere which are part of the assets of the business or profession carried on by the taxpayer (either personally or through a representative) in the Kingdom, subject to the Netherlands part of such activity being considered as a separate enterprise or profession ;
4. All possessions which represent the shares of limited partners in a business which has its seat in the Kingdom and all other property (with the exception of securities) the whole or part of the yield of which depends on the net yield of a business or profession having its seat in the Netherlands.

For purposes of applying the article in question, the term “ business or profession ” does not include salaried employments or functions nor a business or profession which is exercised in the Netherlands merely temporarily and for less than three months.

3. ASSESSMENT OF TAX.

(a) *Computation of Taxable Property and Deductions.**Taxpayers domiciled in the Netherlands.*

The possessions and debts of a married woman are regarded as those of her husband (Article 9 *ter*, paragraph 1), except in the three cases enumerated on page 343 (Article 9 *ter*, paragraph 2).

Assessment is based on the position at the beginning of the tax year (Article 5) — *i.e.*, May 1st (Article 11). In the case of persons whose fiscal liability arises at a later date, tax is assessed on the basis of the position on that date (Article 5).

For purposes of assessment, possessions are divided into three classes: possessions held in full ownership (*pleine propriété*), in usufruct and in mere proprietorship (*nue propriété*). As regards the property of minors, no account is taken of the legal usufruct enjoyed by parents (Articles 4 and 6 (*e*)). The value of usufruct is considered as equal to the amount of capital which would yield an annuity equivalent to 4 per cent of the full-ownership value of the property used. Mere proprietorship of property is equal to the difference between the value of full ownership and the present and future rights of usufruct on the property in question.

In principle, the law taxes the cash value of possessions — *i.e.*, their economic value to the individual taxpayer. In most cases, this economic and individual value obviously cannot be less than the market value, for the taxpayer would otherwise have sold the goods in question. As regards some possessions, however, Article 7 lays down rules which depart somewhat from this principle. Real property is always assessed at its market value ; mortgage debts are assessed at the capital value if the debt and the interest are adequately secured. Securities the value of which is indicated in the last weekly quotation for purposes of computing death duties are assessed for property tax on the basis of this quotation. Annuities are assessed according to the tables contained in Article 47 of the Death Duties Law,¹ when settled upon a single life.

¹ Law of May 13th, 1859 (*Staatsblad*, No. 36).

Deductions. — To obtain the net property, the total value of the taxpayer's possessions is reduced by the actual value of his debts. These debts are dealt with in Article 8 of the Law. Annuities and pensions of all kinds legally due are deducted at their capitalised value, calculated in accordance with the law on death duties. Article 8 of the Property Tax Law prohibits any deduction on the score of a legal usufruct over the taxpayer's property, allowances due in virtue of the provisions in civil law dealing with family relations, future payments not legally due, obligations to continue the maintenance and education of children under age and, finally, life annuities and pensions granted by the taxpayer to his minor children.

Balance-sheet. — Since most traders do not draw up the annual balance-sheet at the end of April, Article 9, in order to avoid the necessity for a fresh balance-sheet, prescribes that the assets of taxpayers who have invested all or part of their estate in one or more enterprises may be assessed on the basis of the last balance-sheet drawn up or approved. These assets, however, must not be represented by negotiable shares; the balance-sheet must show the position of the enterprise at a date not earlier than the preceding tax year, and the taxpayer must be able, if required, to show that the assets and liabilities in the balance-sheet were not so calculated that the surplus is less than would have been obtained by applying the rules of Articles 7 and 8. The amount entered in the balance-sheet is increased or diminished by any amounts that the taxpayer may have added to or withdrawn from the enterprise since the date to which the balance-sheet refers.

Taxpayers not domiciled in the Netherlands.

The rules for assessing the net taxable property of taxpayers not domiciled in the Netherlands are the same as for persons domiciled there, but just as only property deemed to be situated in the Netherlands is taxable, so only debts connected with such property may be deducted from the gross property. These are :

1. Debts secured by a mortgage on real estate situated in the Netherlands ;
2. All debts directly connected with a business carried on by the taxpayer or a representative in the Netherlands or, as the case may be, with a separate enterprise or profession which the part of the business or profession carried on in the Netherlands is deemed to constitute ;
3. Debts which are the result of a participation as limited partner in a business or profession having its seat in the Kingdom (Article 9 *bis*). (For the purpose of applying Article 9 *bis*, see page 355 for the concept of "business or profession".)

(b) *Computation of Tax and Deductions.*

If a married woman not separated from the bed and board of her husband has property separate from the latter's, and if husband and wife both have their fiscal domicile in the Netherlands, tax is computed on the combined net property and is then apportioned according to the separate net property of each party (Article 9 *ter*, last paragraph).

Property tax proper is only levied upon estates exceeding 15,999 florins, and defence tax No. I on estates worth more than 50,999 florins. The rate is given in the Annex.

The principal of the property tax is increased by 55 additional *cents* in favour of the loan fund and, in the case of taxpayers resident in the Netherlands, by the further additional *cents* shown in the Table of Tariffs (see Annex).

Persons who only become subject to tax in the course of the tax year (Articles 1 and 2) pay a tax which is reduced from the normal rate to as many twelfths as there are still months in the tax year to run (Article 11).

Deductions for the Purpose of avoiding Double Taxation.

(a) *Deductions on account of Colonial Taxes.* — With regard to colonial taxes, Article 50 *bis* provides for a deduction similar to that existing in connection with income tax (see page 348). In order that the deduction be applicable, it is necessary that the oversea territory in question levies a property tax. The deduction is applied to both property taxes.

(b) *Deductions on account of Foreign Taxes.* — The decision of the Minister of Finance dated April 17th, 1928 (*Staatscourant*, No. 76),¹ provides, for the purposes of the two property taxes, a deduction on account of direct taxes levied by foreign States both in the case of these taxes being levied on property or on income. (It often occurs that income taxes are not accompanied by property taxes, but that income is treated in a different manner according to its origin. That is the reason why the above-mentioned decision considers that a person chargeable abroad on income derived from property is in reality taxable on account of the property yielding such income.)

This method of deduction is the same as that applied for the purpose of income tax. In other words, it is not a deduction on account of foreign income, but merely an abatement for the avoidance of double taxation. This deduction is applicable to individuals who have had their fiscal domicile in the Kingdom for the previous five years, as well as to other persons of Dutch nationality and to nationals of the States indicated on page 348.

In order to obtain the deduction, the person concerned must be liable to income tax or property tax abroad on account of :

- Real estate situated in the foreign country or ;
- A debt secured by a mortgage on real estate situated in that country or ;
- The carrying-on of a business or profession in that country.

The deduction is equal to the amount of tax which would be due if the taxpayer possessed only property taxable abroad directly (by a property tax) or indirectly (by an income tax) and if his debts were confined to mortgage debts secured on real property situated in the country in question and to the debts directly connected with the business or profession carried on in that country. If real property is situated partly in the Netherlands and partly in the foreign country, the foreign part of the estate is regarded as separate property. The foreign part of a business or profession exercised both within the Kingdom and abroad is regarded as a separate business or profession.

4. COLLECTION OF PROPERTY TAXES. ²

The provisions regarding returns are the same for property taxes as for income taxes. Taxpayers, however, who have received no form of return must apply for one to the inspector (provided, of course, they are actually liable), and in those cases the return must be forwarded to the administration before June 15th. Persons who settle in the Netherlands in the course of the tax year and whose property, combined with that of husband (or wife), amounts to 16,000 florins or more, must declare their property within two months of settlement.

The provisions relating to checking of returns, appeals and payment are similar to the corresponding provisions concerning income taxes.

¹ For legal basis of this decision, see page 348.

² There is no withholding at source.

PART II. — METHODS OF TAXING FOREIGN AND NATIONAL ENTERPRISES

A. FOREIGN ENTERPRISES.

I. DEFINITION AND GENERAL PRINCIPLES.

For purposes of the present survey, a foreign enterprise means any enterprise belonging to an individual or legal entity domiciled¹ for fiscal purposes outside the Netherlands. Under Netherlands law, persons are only liable to tax on the profits and capital of their enterprise if the latter is in more or less permanent "economic contact" with the Netherlands. The following is a complete list of cases in which such contact is held to exist for a person owning an enterprise :

(a) The exercise in the Netherlands of functions or an employment² such as those of managing director or supervisor of a national or foreign share company ;²

(b) The carrying-on of a business or profession³ in the Netherlands.⁴ (We shall revert to this point later, after completing the list. It is of capital importance in Netherlands law, as that law bases the taxation of profits which foreign enterprises derive from the Netherlands on the notion that their owners carry on business there. Thus, it may be said that this last notion fulfils in the Netherlands system the rôle played by "establishment" in the laws of some other countries) ;

(c) The ownership or enjoyment of, or a property right to, real property situated in the Netherlands or the possession of a mortgage on such property ;⁵

(d) Enjoyment of legal usufruct on real property situated in the Netherlands or on a mortgage debt secured on such property ;⁶

(e) Rights to shares in the net profits of an enterprise or liberal profession, of which the centre (seat) of the activities is in the Netherlands,⁷ in virtue of a claim other than remuneration for the fulfilment of functions or employment or the possession of securities ;⁸

(f) The right to a share of income from an employment or functions the centre (seat) of which is in the Netherlands ;⁹

¹ For fiscal domicile of individuals, see page 340 ; for that of legal entities, see page 335.

² Income Tax Law, Article 2 (c).

³ Fiscal liability exists whether the business or profession is carried on personally or through representatives ; but if the activities in the Netherlands are purely temporary and exercised for less than three months, no tax is imposed. It should be noted that profit-making activities outside of a regular business or profession by persons not domiciled in the Netherlands are not taken into account.

⁴ Income Tax Law, Article 2 (c) ; Property Tax Law, Article 2 (c).

⁵ Income and Property Tax Laws, Article 2 (a) and (b) ; Land Tax Law, Article 47.

⁶ Income Tax Law, Article 2 (a) and (b).

⁷ If the activities mentioned above are exercised only temporarily within the Netherlands, no tax is levied ; Income Tax Law, Article 2 (d), and Property Tax Law, Article 9 bis.

⁸ Income Tax Law, Articles 2 (d) and 24, No. 2 ; Property Tax Law, Articles 2 (d) and 9 bis.

⁹ Income Tax Law, Article 2 (d) ; property tax is in this case not levied, as expressly stipulated in Article 9 bis, last paragraph, of Property Tax Law.

(g) The enjoyment of profits or salaries distributed or paid by share companies, limited partnerships with share capital, co-operative and other societies and mutual insurance companies, the fiscal domicile of which is in the Netherlands.

In order that a foreign enterprise may be liable to *land and buildings tax*, it must, and need only, enjoy under a property right real property situated in the Netherlands. If the enterprise belongs to a partnership, it is the partnership itself that is liable,¹ contrary to what is the case in regard to income and property taxes.

Foreign enterprises which receive profits distributed by Netherlands companies (case (g) above) are not themselves liable to the *tax on dividends and tantièmes*. This tax is paid by the Netherlands company. (This does not prevent owners of foreign enterprises being personally liable to income tax on these same distributions and salaries in cases (a) to (f). See below.) It does not matter whether the foreign enterprise receiving distributions subject to the tax on dividends and *tantièmes* has or has not an establishment in the Netherlands, but, in the case of salaries subject to this tax, account should be taken of the form of the enterprise to which these salaries are paid, since exemptions from this tax are differently reckoned according as the enterprise in receipt of this income is or is not a partnership.²

For purposes of *income and property taxes*, enterprises belonging to partnerships are regarded as owned by the partners themselves, who are held personally liable for the tax.

Foreign enterprises coming under cases (a), (b), (c), (d) and (f) of the above list are liable to income tax, and those coming under cases (b), (c) and (e) are liable to property tax.

As already mentioned, Netherlands law makes the tax liability of enterprises doing business in the Netherlands depend, not upon the existence of an establishment in the Netherlands, but rather upon the "carrying-on of a business or profession" in the country. The carrying-on of a business or profession (*bedrijf of beroep*) includes all commercial and industrial undertakings (including banking, insurance, transport and real estate enterprises), mining, agriculture, forestry and fishing; all liberal professions (e.g., medicine, law), as well as functions and employments other than liberal professions, functions and employments. The law does not define the term "*bedrijf*" (the carrying-on of a business, including agriculture). It should be noted here that an enterprise may be regarded as carrying on business in the Netherlands, even if the operations it conducts there are only a special part of its normal activities.³

Administrative practice interprets the expression "carrying on a business or profession in the Netherlands" as meaning that the activities in question represent a more or less regular "economic contact" on a scale of some importance with the Netherlands. Among the many examples of such contact may be mentioned the existence in the Netherlands of a factory, works, yard, mine, farm (worked, of course, by the enterprise), railway or tramway lines, halting-place or landing-stage of land or water transport; the booths and tents of circuses and fairs; workmen employed by a contractor who has contracted for work in the Netherlands; an office used by an enterprise directly or by one of its employees; an agent with power to deal in the name of the enterprise or a person who, although not having power of attorney, is nevertheless the enterprise's employee.

Further, any person is regarded as having regular economic contact with the Netherlands who comes there regularly on business or in the exercise of a profession; this covers itinerant traders.

2. TAXATION OF CERTAIN KINDS OF INCOME AND PROPERTY.

We shall discuss the taxation of the various kinds of income and property that foreign enterprises may enjoy in the Netherlands in the light of Articles 24 of the Income Tax Law and

¹ See page 333.

² See page 335.

³ In support of this interpretation, see Article 36 of the Income Tax Law and Article 9 *quinquies* of the Property Tax Law, which exempt foreign banks of issue operating in the Netherlands, and Article 3 of the Income Tax Law, which exempts foreign shipping companies whose vessels ply between the Netherlands and foreign countries.

9 *bis* of the Property Tax Law. The former article, however, must be interpreted in conjunction with Articles 5 to 8 of the same law¹ and of the jurisprudence in relation thereto.

(a) DIVIDENDS.

It will be remembered that dividends distributed by companies the fiscal domicile of which is in the Netherlands are liable to the *tax on dividends and tantièmes*, which tax is paid by the company distributing the dividends, that company having no claim for tax against the persons to whom these dividends accrue.

As to a foreign enterprise which would enjoy such dividends, its owner would be subject to *income tax*, like any other taxpayer, not only on the said dividends, but on dividends accruing to the enterprise from colonial and foreign companies, provided they represent part of the income on account of or in connection with the carrying-on of business in the Netherlands. The dividends in question are regarded not as "income from capital" proper, but as income attaching to the carrying-on of business. Such is the case where investments or reserves are concerned, or where the enterprise has bought securities with a view to exercising a control in a company with which it has business relations, or finally for the investments of a bank.

If the dividends are liable to income tax, the securities on which they are paid are liable to property tax.

(b) INTEREST.

Owners of foreign enterprises are liable to income tax in respect of interest on bonds, mortgage debts or any other secured or unsecured debts — wherever the debtor's seat of business or domicile is and wherever the place of payment may be — if such interest is to be regarded as acquired on account of or in connection with the carrying-on of business in the Netherlands.

If interest is liable to income tax, the capital from which it is derived is liable to property tax after deducting any liabilities with which it is charged.

If a foreign enterprise not carrying on business in the Netherlands enjoys interest on debts secured on real property situated in the Netherlands, that interest is taxable there as yield from capital,² unless it is to be considered as income from carrying on a business or profession (*e.g.*, in the case of a mortgage bank). Further, and not subject to this restriction, these mortgage debts are liable to property taxes without any deduction. The interest and principal of sums lent or entrusted without mortgage security to a person domiciled in the Netherlands by an enterprise coming under the conditions mentioned in this paragraph (*i.e.*, not carrying on business in the Netherlands) are not taxable.

It should be added that if the reward of capital lent by a company liable to the tax on dividends and *tantièmes* is not fixed in amount, but varies with the profits of the borrowing company, the latter has to pay the tax on dividends and *tantièmes* on this interest.

(c) DIRECTORS' PERCENTAGES.

We do not propose to revert to what was said in dealing with the *tax on dividends and tantièmes* as to the taxation of percentages and salaries of the directors of Netherlands companies. It must, however, be mentioned that Article 9 *bis* of the law on dividends and *tantièmes* exempts from tax

¹ See page 347.

² Income Tax Law, Article 24, No. 2.

the whole of the percentages and salaries payable for functions exercised outside the Netherlands. If this exemption is to apply, these functions must, of course, be such as would necessarily have to be exercised in the colonies or abroad.

As regards *income taxes*, percentages and salaries of directors, etc., are taxable in so far as the directors discharge their duties in the Netherlands (see (g) below).

(d) ROYALTIES FOR THE USE OF PATENTS, COPYRIGHTS, TRADE-MARKS, SECRET PROCESSES AND FORMULÆ AND SIMILAR INCOME.

Netherlands share companies, which pay royalties for the use of patents and other intangible personal property or for the use of secret processes conceded or entrusted to them by foreign enterprises, do not have to pay the *tax on dividends and tantièmes* on these royalties unless the latter are in one way or another dependent upon the net profits of the enterprise. If royalties, without being formally dependent upon the conceding company's profits, are fixed at an abnormally high figure, the fiscal authorities regard them as assimilable to distributions of profits liable to the tax on dividends and *tantièmes*, whenever the conceding enterprise directly or indirectly possesses a substantial part of the shares of the concessionary company. All these rules apply both when the conceding company is a foreign enterprise and when it is a person domiciled in the Netherlands.

As regards a foreign enterprise in receipt of these royalties, it will be subject to income taxes if the royalties are part of receipts connected with the carrying-on of business taxable in the Netherlands. On the contrary, royalties are never subject to these taxes in so far as they can be considered as derived on account of or in connection with the carrying-on of business outside the Netherlands. As regards other royalties, their foreign recipients will only be taxable in cases where the two following conditions are fulfilled: (1) the source of the royalty should be the object of a property right; and (2) the royalty should itself depend on the net profits of a business or professional activity which has its seat in the country (Income Tax Law, Article 24, No. 2). When the royalties only depend in part on the net profit of such business activity, they are only partly taxable. It should be noted that the contractual right to a royalty granted in consideration of the entrusting of secret formulas or processes is to be regarded as intangible property. The property from which royalties subject to income taxes arise is subject to property taxes. Even if the royalty cannot be considered as part of the business income of the recipient, the entire value of the property, provided it is a right recognised by the law, from which it is derived will be taxable, even if the royalty itself is only in part subject to tax (Property Tax Law, Article 9 *bis*, paragraph 1, No. 4).

(e) RENTS FROM REAL ESTATE, MINING ROYALTIES AND SIMILAR INCOME.

Every foreign enterprise, which in virtue of a property right enjoys real estate situated in the Netherlands, is liable in respect thereof to *land tax*, which is assessed on the cadastral income of the property.

As regards *income taxes*, income derived by a foreign enterprise from real estate is taxable both in the case where the property is situated abroad or in the Netherlands, when this income is obtained on account of or in connection with the carrying-on of business taxable in the Netherlands. Moreover, even if the enterprise does not carry on business in the Netherlands, it will be liable to income tax in respect of income from any real estate it owns there, unless this income should be considered as income connected with the carrying-on of business abroad. In cases where the properties, but not the business, should be considered as the separate source of the income, it should be noted that the interest from any mortgages on these Netherlands properties will be deducted from the total amount of the net income from taxable sources.

The foreign enterprise will be liable to *property taxes* on the value of all its real estate in the Netherlands and on the value of its other real estate if it is liable to income tax on the income from such estate. Before tax is levied, any mortgage debts on the properties situated in the Netherlands will be deducted. Further, if the enterprise carries on business within the Netherlands, debts incurred in connection with the carrying-on of such business taxable in the Netherlands¹ will be deducted from the value of its real estate, as from the value of any other kind of assets.

(f) GAIN DERIVED FROM THE PURCHASE AND SALE OF REAL ESTATE, SECURITIES AND PERSONAL PROPERTY.

In the light of Articles 24 and 7 of the Income Tax Law, persons having their fiscal domicile outside the Netherlands are not liable in respect of profits from transactions in real or personal property, tangible or intangible, if the transactions are unconnected with the enterprise or profession in which the persons are engaged.

If a foreign enterprise derives gain from the purchase or sale of real estate, securities and other personal property, it is liable to tax if these profits are part of the receipts from the carrying-on of business within the Netherlands.

When part of the property connected with the carrying-on of such business (real property, equipment, etc.) is sold for a sum exceeding its book value, the excess is regarded as taxable profit. The Finance Minister, however, has ruled that the gain realised by a farmer from the sale of land used in his undertaking shall not be considered as taxable profits. But this decision, which is only binding upon the administration, does not prevent farmers from getting losses on such sales declared by the judge (Board of Appeals) to be deductible losses.

Administrative practice considers gains from the purchase or sale of real estate as earned in the country where the estate is situated, and gain from the sale or purchase of securities as earned in the country which initiated the sale.

With regard to other personal property, a distinction is made according as the enterprise does or does not carry on business in the Netherlands. If it does, the profits from sales effected as part of the enterprise's Netherlands activities are regarded as taxable in the Netherlands. Otherwise, they are exempt. But if the purchase effected by the Netherlands part of the enterprise demanded a certain degree of commercial skill and ability, a part of the profit is considered as due to the purchase and is taxed in the Netherlands.

It should be added that, generally speaking, the fiscal authorities attach far more importance to the place where transactions are initiated or completed than to the place where they are formally concluded. Further, if the goods sold were manufactured by the enterprise itself, a part of the profit is ascribed to the country of manufacture.

(g) SALARIES, WAGES, COMMISSIONS AND OTHER REMUNERATION FOR SERVICES
(INCLUDING DIRECTORS' SALARIES AND FEES).

If the above-mentioned income is distributed by a Netherlands company, it is in principle subject to the *tax on dividends and tantièmes*, provided it exceeds a certain sum. This tax, as we have said, is paid by the company.

The recipient of such income is liable to *income tax* on it, even if he has his domicile abroad, if the income corresponds to the carrying-on of a business or profession in the Netherlands by himself or his representative. And, if the remuneration represents work done partly in the Netherlands

¹ See Property Tax Law, Article 9 *bis*.

and partly elsewhere, tax is only imposed on the part corresponding to work actually accomplished in the Netherlands.

(h) INCOME FROM A TRUST.

Trusts are unknown in Netherlands law and there are no special rules for their taxation.

(i) INCOME FROM CARRYING ON A BUSINESS OR INDUSTRY THROUGH :

1. *A Local Commission Agent or Broker.* — If a foreign enterprise does business in the Netherlands only through a local commission agent or broker, it is not liable to income or property taxes since it cannot be regarded as carrying on business within the country, even if it regularly entrusts goods to a commission agent or from time to time to a broker.

2. *A Local Dealer or Distributor.* — A foreign enterprise would be considered as carrying on business in the Netherlands only if these middlemen were bound to confine their activities exclusively to selling the enterprise's goods.

3. *A Travelling Salesman, whether or not having Power to conclude a Contract.* — The enterprise is only liable to tax in the Netherlands on the carrying-on of business if the salesman's power of attorney enables him to effect more than one kind of operation (sale, purchase, delivery, acceptance, collection, payment).

4. *A Local Agent with Power of Attorney.* — If the agent's power of attorney authorises him to engage in various operations (see above), or if he is required to represent the enterprise exclusively, the latter is liable.

5. *An Agent selling out of a Stock belonging to the Foreign Enterprise.* — If such agent is authorised to sell or buy in the enterprise's name or to collect or pay money on its account, the enterprise is liable. So it is if the agent is required to serve the enterprise exclusively. In these cases property tax is levied on the stocks and warehouses belonging to the enterprise.

6. *A Permanent Establishment of Any Kind.* — In such cases the enterprise is regarded as carrying on business in the Netherlands ; it is therefore liable.

B. NATIONAL ENTERPRISES.

1. DEFINITION AND GENERAL PRINCIPLES.

For our present purpose a national enterprise means any enterprise belonging to an individual, a share company or a foundation domiciled for fiscal purposes in the Netherlands.

If these enterprises belong to individuals (or to partnerships), the owners are liable to income and property taxes. Such persons are in principle liable both in respect of their foreign income and property and in respect of income and property they enjoy in the Netherlands. But, as already mentioned, if the foreign income or capital is liable to a foreign tax on income or property and if certain other conditions are fulfilled, these enterprises are exempt from the Netherlands income tax proper (by means of a deduction) and from the two property taxes in respect of such income and capital (see pages 348 and 353). On the other hand, in so far as colonial taxes are concerned, the fact that a colonial income tax is levied entails a deduction only as regards income tax, and likewise the fact that a property tax is levied in Netherlands East India entails only a similar deduction for the purpose of property taxes. If these enterprises belong to foundations, the latter are liable to income tax proper in respect of all their profits ; the above deductions do not apply to their case.

In the case of share companies and other associations liable to the tax on dividends and *tantièmes*, that part of their distributions which is derived from abroad or from overseas territories is, as already mentioned, only taxed as to one-third of it (see pages 337 and 338).

After thus indicating the general principles which follow from what was said in Part I of the present survey, we must now make a few further observations as to the influence which taxes due abroad have on taxation in the Netherlands.

1. Only taxes due to a foreign *Government* are taken into account. Local taxes justify no deductions whatever. In principle, no deduction is allowed in respect of any foreign taxes not owing by the taxpayer personally. This rule is subject to two exceptions :

Members of an ordinary or a limited partnership are entitled to a deduction on the score of taxes paid abroad by the partnership to which they belong, just as if these taxes were imposed upon them directly.

Further, if a share company receives dividends from a foreign company, it may claim a deduction on the score of taxes to which the foreign company is liable in respect of its profits in the country of its domicile. This deduction, however, cannot be claimed if the tax due from the foreign company is in one way or another dependent upon the fiscal domicile of its shareholders.

2. In connection with deductions and abatements for the purpose of property tax, foreign taxes on income are assimilable to taxes on property. The same is reciprocally true as regards income tax. These assimilations do not take place, however, in so far as colonial taxes are concerned. ¹

3. A land and buildings tax of the same nature as the Netherlands land and buildings tax, which is not, properly speaking, part of a system of impersonal taxes, does not allow the taxpayer to claim a deduction of tax on the score of it.

2. TAXATION OF CERTAIN KINDS OF INCOME.

(a) DIVIDENDS.

The fiscal regime for foreign dividends accruing to Netherlands enterprises differs according as the owners of these enterprises are by reason of their status liable to income tax or to tax on dividends and *tantièmes*.

As regards *income taxes*, dividends received from abroad are taxable and are treated exactly like dividends paid in the Netherlands. The fact that they have been subject to a tax of some kind abroad only allows the taxpayer to deduct the tax paid abroad from the taxable dividend. No other deduction or exemption is allowed. If, however, these dividends are to be regarded as part of the receipts from carrying on business abroad, they will, in certain circumstances, be exempt from Netherlands income tax proper. ²

The position as regards *dividends and tantièmes* tax is quite different. Only a third part of the profits distributed by the Netherlands company which corresponds to the dividends it has itself derived from abroad is taxed. This exemption does not overlap the exemption of income from the carrying-on of business abroad, for, in assessing tax, these dividends are distinguished and kept separate from other foreign income.

As regards *property taxes*, securities are only exempted when the dividends they yield are themselves exempted from income tax.

(b) INTEREST.

As regards liability to the different taxes of interest derived by Netherlands enterprises from abroad and of the personal property which produces this interest, two main cases must be distinguished.

¹ Such is the case, in particular, as regards taxation of property subject to property tax in the Netherlands, the income from which property has already been charged with income tax in Surinam and Curaçao, where there is no property tax.

² See "General Principles" above and pages 348 and 349.

First, interest from abroad received on account of or in connection with the carrying-on of business ; and, secondly, interest which should be considered as mere income from capital.

In the case of interest and debts coming within the first category, there is no fixed rule for determining whether they relate to the Netherlands or to the foreign part of the enterprise, the debtor's domicile and the place of payment being in principle immaterial.

In the absence of more definite evidence, the tendency is to ascribe such interest and debts to the part of the enterprise with which the debtor is in the closest touch.

Interest which should be considered as representing profits from the carrying on of business is treated like other profits from such business, whatever the debt to which they refer and whatever the terms and security of the debt, and, if it is ascribable to the foreign part of the enterprise, it will enjoy the preferential treatment accorded to business income derived from abroad.

For purposes of the *tax on dividends and tantièmes*, only interest which may be considered as representing income from the carrying-on of business may be included in the fraction referred to in Articles 27 and 28 of the Law, briefly, in the dividends and percentages taxable to the extent of one-third only, as having their origin in income from carrying on business taxable abroad or in the colonies (see pages 337 and 338).

For the purpose of *income and property taxes*, a distinction should be made as regards mere investments of capital according as they do or do not correspond to mortgages on real estate abroad. If they so correspond, the person concerned may claim the ordinary deductions allowed on the score of foreign taxes (see pages 347-349 and 353).

Other interest, whatever the debt to which it refers, may lay no claim to deductions, and the only advantage the taxpayer can claim from the taxation of his interest is that he can deduct from its total the amount of foreign tax paid.

(c) DIRECTORS' PERCENTAGES.

Individuals receiving directors' percentages from abroad for functions discharged there may claim income-tax abatement if the remuneration of these functions is liable to income tax in the country where they are discharged. Such percentages paid to Netherlands companies are regarded as earned in the country where the functions, the remuneration of which they represent, were discharged and may claim the benefit of the ordinary deductions allowed to profits derived from abroad.

(d) ROYALTIES FOR USE OF PATENTS, COPYRIGHTS, TRADE-MARKS, SECRET PROCESSES AND FORMULÆ AND SIMILAR INCOME.

Any individual domiciled in the Netherlands and liable to income tax proper may claim the income-tax deduction allowed in respect of income from abroad, in the following cases :

Enjoyment of royalties from patents or other intangible personal property, if these royalties are part of profit derived on account of the carrying-on of business abroad ;

Enjoyment of royalties in virtue of a right constituting intangible property depending upon the results of an enterprise having its seat abroad and belonging to a third person.

The value of the patent or right itself, if it constitutes property recognised by the law, is subject to *property taxes*, but the deductions on the score of foreign holdings are granted in the same cases as in those which give right to a deduction on this account as regards income tax.

From the point of view of *dividends and tantièmes*, royalties paid abroad to a Netherlands company are taxable at the time of their distribution. In the cases, however, where they can be regarded as belonging to the foreign part of the enterprise, they will enjoy the deductions generally allowed to distributions of foreign origin liable to this tax. There are no strict rules where it is a

matter of doubt whether the royalty for use of a patent is to be regarded as part of the income ascribable to the foreign country or to the Netherlands. As a matter of guidance, however, it may be said that, when the royalty depends upon the profits of the foreign concessionary company abroad, it would be considered as foreign income, but, when it is a fixed sum, it is likely to be regarded as part of the income ascribable to the Netherlands.

(e) RENTS FROM REAL ESTATE, MINING ROYALTIES AND SIMILAR INCOME.

With regard to the above-mentioned income, a distinction must be made between the case where it consists of rent from property not used by the taxpayer in the carrying-on of his business or from property which is so used.

In the former case the taxpayer may claim in respect of the *income* from this property the deductions generally granted in respect of foreign income. It should be specified that, for the purposes of computing this deduction, interest from any mortgages on the property will be deducted from the income.

The abatement in favour of foreign income is also allowed when the real estate is used for foreign business purposes — *i.e.*, when the income from this estate is part of the profit earned in the country where the estate is situated. In computing these foreign profits, however, only interest on debts incurred in connection with the carrying-on of business abroad may be deducted from the gross profits. Hence, if the taxpayer mortgages estate used in the carrying-on of his foreign business, in order to buy a house for his private use in the Netherlands, no deduction will be allowed.

As regards *property taxes*, owners of real estate abroad may claim the ordinary deduction allowed in favour of foreign property. The deduction is computed after subtracting any mortgage debts of the taxpayer on the property. If the estate in question is part of assets used for the carrying-on of business abroad, the deduction of debts is independent of whether they are mortgage debts or not. They need only be debts incurred in connection with the carrying on of business.

In the case of the *tax on dividends and tantièmes*, income from real estate situated abroad is a factor in determining the foreign income on which is based the deduction allowed to companies that derive part of their income from abroad. Such is not the case, however, if such income is not part of the business profits of the enterprise.

(f) GAIN DERIVED FROM THE PURCHASE AND SALE OF REAL ESTATE, SECURITIES AND OTHER PERSONAL PROPERTY.

If gains under this heading accrue to an individual domiciled in the Netherlands, they are taxable : (1) if they are earned in the course of carrying on business, even though the gains were neither sought nor expected ; (2) if the operation resulting in gain, although not in pursuance of the individual's usual business, is something more than an occasional act of speculation.

In the second case, the gain is taxable without any deduction on the score of direct taxes which would be due abroad ; any duties or taxes on the operation itself are of course deducted from the gain. In the other case, the taxpayer is entitled to the deduction ordinarily allowed in respect of income from carrying on business or a profession abroad (as regards the allocation of these gains to the Netherlands or to the foreign country, see page 358).

With reference to the tax on *dividends and tantièmes*, the same principle applies, *mutatis mutandis*, as was explained in regard to the first of the two above cases.

(g) SALARIES, WAGES, COMMISSIONS AND OTHER REMUNERATION FOR SERVICES.

The fiscal regime for salaries, wages and commissions is similar to that described in connection with directors' percentages (see page 361).

(h) INCOME FROM A TRUST.

Netherlands law is unacquainted with the trust idea. Nothing therefore need be said about trusts here.

(i) INCOME FROM CARRYING ON A BUSINESS OR INDUSTRY THROUGH :

1. *A Local Commission Agent or Broker.* — In this case, as in those which will be dealt with below, the main question to be considered, both in regard to income and property taxes and the tax on dividends and *tantièmes*, is whether the taxpayer is to be regarded as carrying on business abroad (in this connection see page 355).

If the owner of the enterprise is on this account liable to tax abroad, the general deductions laid down for income tax and dividends tax apply in this as in the other cases.

Enterprises which carry on business through the special intermediary of a broker or commission agent cannot be regarded as carrying on business abroad. The same applies even to an enterprise which regularly entrusts goods to a commission agent or from time to time to a broker.

2. *A Local Dealer or Distributor.* — An enterprise is held to be carrying on business abroad only if these middlemen are required to devote themselves exclusively to the sale of the enterprise's products.

3. *A Travelling Salesman, whether or not having Power of Attorney.* — In such cases there is held to be no carrying-on of business (in the sense of which we are speaking) unless the salesman's power of attorney allows him to effect more than one class of transactions (sale, purchase, delivery, acceptance, collection, payment). Subject to this restriction, the whole of the profits from operations concluded by such travelling salesman will be taxed in the Netherlands.

4. *A Local Agent with Power of Attorney.* — If the agent is authorised to conclude various operations (see above), there is a carrying-on of business abroad, and the deductions generally allowed in respect of income derived from abroad will apply.

5. *An Agent selling out of a Stock belonging to the Foreign Enterprise.* — In order that there may be a carrying-on of business abroad, the agent must be buying or selling in the enterprise's name or must be collecting or making payment on its account or must be required to work exclusively for the enterprise.

For purposes of property tax, any stocks and warehouses in this agent's keeping will be taken into account in reckoning the deductions generally granted in favour of property situated abroad.

6. *A Permanent Establishment of Any Kind.* — If an enterprise has a permanent establishment abroad, it is regarded as carrying on business there. A decision of 1928 has laid down that, for purposes of the deductions to be allowed in respect of income and property tax, the foreign establishment shall be regarded as a separate enterprise.

As regards *dividends and tantièmes tax*, the law refers to the Income Tax Law for the computing of profits derived from carrying on business abroad.

PART III. — METHODS OF ALLOCATION

A. FOREIGN ENTERPRISES WITH A LOCAL BRANCH OR SUBSIDIARY IN THE NETHERLANDS.

I. GENERAL QUESTIONS AND METHODS OF APPORTIONMENT.

(a) BOOK-KEEPING AND ACCOUNTING REQUIREMENTS.

Netherlands fiscal law lays down no provisions as to the manner in which taxpayers should keep their accounts, and the only regulations on this matter are those contained in the Commercial Code.

Article 6 of the Code prescribes in the first place that every trader shall keep records which show the situation in regard to his property and everything relating to his activities, and indicate at any moment his assets and liabilities. Under the same article every trader must, within the first six months of each year, draw up a balance-sheet according to the requirements of his business, and sign it in his own handwriting. It further lays down that the books and documents containing these records, and the balance-sheets, must be kept for thirty years and that all letters and telegrams received and copies of letters and telegrams despatched must be kept for ten years. Article 42 of the same Code imposes upon the directors of Netherlands share companies the duty of drawing up an annual balance-sheet and profit-and-loss account within eight months of the closing of the company's business year, unless the general meeting of shareholders for special reasons extends this term. In the case of those forms of share company which are required to file a copy of their balance-sheet and a statement of their estimates and profit-and-loss account to the Register of Commerce (Article 42 (c)), this balance-sheet must make separate mention of : sums and other receivables payable at sight by banks and credit institutions; the holdings in other enterprises and debts owed by the latter ; the securities owned by the enterprise ; all claims other than those mentioned above ; the enterprise's stocks, real property and equipment used in the business ; intangible property not already mentioned ; debts payable on notice ; losses and expenditure carried forward to the next business year ; and, lastly, the balance payable on shares subscribed for by the shareholders.

From the fiscal standpoint, however, these provisions are of limited importance. For while fairly primitive accounts may be accepted as satisfactory, accounts kept in absolute accordance with commercial law and acceptable to the ordinary courts may be rejected by the fiscal administrative and judicial authorities.

(b) METHODS OF ALLOCATION.

I. *Method of Separate Accounting.*

It is a principle of Netherlands fiscal law to tax the branches of foreign enterprises on the basis of their own results. There are only few exceptions to this rule and we shall deal with them later. It follows, therefore, that if a foreign enterprise keeps, for its branch situated in the Netherlands,

satisfactory accounts showing the branch's exact position, the administration naturally takes its stand on the data furnished by these accounts and assesses tax on the results as shown therein. Even if certain items do not appear to have been estimated satisfactorily, the administration will still accept the accounts as the basis of taxation after making certain necessary corrections. For this purpose it will compare the position of the branch in question with that of other taxpayers engaged in the same kind of trade or industry. It will check whether the prices at which the foreign enterprise has invoiced its branch are normal, making use of all available information at its disposal, such as Customs declarations, experts' affidavits, etc.

It should be noted that this method of separate accounting is never applied to foreign railway or tramway companies whose lines cross the frontier, nor to insurance companies. These enterprises are taxed by empirical methods or by fractional apportionment.

2. *Empirical Methods.*

The law, as we have just said, provides for the use of empirical methods in the case of two kinds of enterprise. Further, even where there is no such provision, profits can be determined by this empirical or "presumptive" method, if the accounts do not seem to offer a satisfactory basis. In such cases the companies will be assessed on the basis of a comparison with national enterprises operating under the same conditions, and, for this purpose, recourse will be had to turnover, amount of investments, the net amount of the assets destined for the Netherlands part of the enterprise, number of employees, etc. It is impossible to go into detail, as the application of these methods varies from case to case. We shall explain the empirical methods applied, for purposes of income tax, to international railway and tramway companies and to insurance companies (except when the latter prefer to be taxed by the method of fractional apportionment) under the headings specially devoted to these enterprises.

3. *Method of Fractional Apportionment.*

The law prescribes this method only in the case of insurance companies; moreover, the company must request the use of the method. Practical necessity, however, has led the administration to apply this method, combined with that of separate accounting, to other enterprises as well. To be more accurate, the administration does so almost always in the case of banks and hardly ever in other cases. If the method of separate accounting were alone used, it would sometimes be very difficult to allocate some of the items serving to determine capital and profits. This is particularly the case with regard to debts due or owed by the enterprise, and interest thereon. We shall see in what manner use is made of this method when we deal with the apportionment of liabilities of banking enterprises (see page 370) and with the apportionment of liabilities and assets of foreign insurance companies (see page 372).

4. *Requirements for Selection of Methods and Value of the Various Methods.*

In principle, unless the law provides otherwise, as in the case of insurance companies, neither the taxpayer nor the administration has the right to employ the method of fractional apportionment in so far as the question is that of determining the entire profits and capital taxable in the Netherlands. The taxpayer and the administration are not, however, forbidden to agree that this method will be applied. Moreover, if the administration, in the course of proceedings before the Appeal Board, proves that the fractional method is the only satisfactory one, the assessment made in accordance with this method will be upheld. Otherwise, attempt will be made to determine the

branch's taxable profits and capital on the basis of the accounts and, if this is impossible, recourse will be had to a comparison with similar national enterprises, or the gross Netherlands profits will be estimated and deduction made of the working costs of the Netherlands part of the enterprise.

The most satisfactory method is that of separate accounting. This includes also any determination of the profits, which, being made in the absence of sufficient separate accounts, may be considered as leading to the same results that would have been arrived at had it been possible to base a determination on such accounts.

Empirical methods have one advantage — their simplicity. Fractional apportionment is specially suited to financial and banking concerns and, as regards property taxes, to insurance companies, when they have in the Netherlands not a mere agency but an important branch.

(c) APPORTIONMENT BETWEEN BRANCH AND PARENT ENTERPRISE.

I. *Apportionment of Gross Profit of Local Branch to Real Centre of Management abroad.*

Generally speaking, there is no such apportionment. But it may happen that part of the branch's gross profits is indirectly ascribed to the parent enterprise under the fractional apportionment method.

2. *Apportionment of Expenses of Real Centre of Management to Branch.*

Interest Charges.

Interest charges on general indebtedness of the enterprise as a whole are only apportioned in whole to the Netherlands in so far as these debts were contracted for the purposes of business within the country.

As regards property tax, the principal itself of such debts will be deducted from the Netherlands assets to the extent that the proceeds of the loan were devoted to the Netherlands part of the enterprise. On the other hand, even if the proceeds of the loan were devoted to another purpose, any mortgage debt secured on real estate in the Netherlands will be deducted from the Netherlands assets of the enterprise.

General Overhead.

The general overhead expenses of a real centre of management abroad are only deducted from the profits of the Netherlands branch in so far as they directly relate to the activities of that branch. Although this is more a matter of making such a fact plausible than formally to prove it, it is rare that the taxpayers show to the satisfaction of the fiscal authorities that general overhead expenses incurred abroad relate to Netherlands activities. Quite often, too, there is no need to make a special deduction of general overhead of the real centre of management, because these expenses are included in the invoice prices from the principal establishment to its Netherlands branch.

3. *Apportionment of Net Profit.*

As regards the taxation of a branch of a foreign enterprise, income-tax law does not prescribe, when assessing a branch belonging to a foreign enterprise, the taking into account of losses or profits which the enterprise may have realised elsewhere than in the Netherlands. The practice is different when the method of fractional apportionment is employed. In such cases the results of the foreign part of the enterprise necessarily affect the amounts taxable in the Netherlands.

These remarks also apply, *mutatis mutandis*, to property taxes. The losses incurred by an enterprise anywhere diminish its capital, and losses suffered abroad may therefore indirectly affect the computation of property taxable in the Netherlands.

(d) APPORTIONMENT BETWEEN PARENT ENTERPRISE AND SUBSIDIARIES.

In principle, the fact that a Netherlands share company is a subsidiary of a foreign enterprise does not involve any departure from the rules applying to the taxation of the company's profits.

Thus the subsidiary will be liable to the tax on dividends and *tantièmes* like any other Netherlands share company, distributions accruing to the parent company being taxed according to the rules common to all distributions. On the other hand, the parent company will not have to pay income tax in respect of the deriving of dividends,¹ or property taxes on shares held, since, as we have already explained, foreign enterprises are not liable to these taxes through merely receiving Netherlands dividends or holding shares in Netherlands companies.

But it should be noted that a subsidiary may happen to pay abnormally high amounts in consideration of the supply of goods or the rendering of services, or as the result of some other transaction. In this case, the authorities regard any amount which, in the light of the subsidiary's accounts and other data at its disposal, appears to it to be in excess of the normal as a distribution of profits and subject on this account to the tax on dividends and *tantièmes*.

Possibly, too, the Netherlands fiscal authorities will regard the subsidiary as being in reality but a mere branch. Here, two cases must be clearly distinguished. In the first place, the persons whose names appear as the founders of the Netherlands subsidiary company may, in fact, have lacked the will to effect a joint venture² or there may have been only one real founder. In such case, the company is ignored, without special procedure, for purposes of taxes on dividends and *tantièmes*, income and property; the fact is that the subsidiary company does not exist, as it has not been validly incorporated. On the other hand, in the case where the incorporation of the company is not clouded, the fiscal authorities are allowed to disregard it for purposes of the so-called personal tax³ and the taxes on income and property, if the founders, in creating the company, intended to deprive the fiscal authorities of revenue from these taxes and provided that without this purpose they would not have organised the company (Law of April 29th, 1925, *Staatsblad*, No. 171). This law prescribes a special procedure in such cases. It does not apply to the tax on dividends and *tantièmes*. That tax, therefore, is always collected if the company has been legally incorporated, even when the founders are themselves liable to income and property taxes in respect of the branch which is deemed under the Law of April 29th, 1925, to belong to them.

II. APPLICATION OF THE METHODS OF ALLOCATION IN SPECIFIC CASES.

(a) INDUSTRIAL AND COMMERCIAL ENTERPRISES.

I. *Selling Establishments.*

Local Establishments selling in National Markets.

When a foreign enterprise has a selling establishment in the Netherlands, it does not matter whether the goods sold by that establishment have been manufactured or merely bought abroad by the main enterprise. The only question which arises is whether the goods have been invoiced to the

¹ For the percentages which the parent company would enjoy, see pages 356 and 358.

² This intention is under Netherlands law an essential of the company contract.

³ The present survey does not deal with the so-called personal tax. This tax is assessed on certain expenses of the taxpayer.

Netherlands establishment at the normal price — that is, the price which would have been fixed had the establishment bought them from a separate enterprise.

The gross profits, from which the net taxable profits are calculated in accordance with the ordinary rules, are obtained by deducting this price from the gross receipts of the establishment. Sometimes, when it is difficult to determine the normal invoice price, the selling profit is fixed at a fraction — say, half —¹ of the gross profit resulting from both manufacture and sale.

Local Establishment of Foreign Enterprises selling abroad.

If the Netherlands branch of a foreign enterprise sells in a colony or foreign country where the enterprise cannot be said to carry on business, the sale profit will be ascribed to the Netherlands branch. As already mentioned on page 358, the Netherlands fiscal authorities are inclined to consider sale profits as attributable to the country where the sale was prepared and negotiated rather than to the place in which the transaction was formally concluded.

2. *Manufacturing Establishments.*

If a foreign enterprise produces at a factory or other industrial establishment in the Netherlands goods which it sends to another country where it also carries on business, and if the goods are sold in that country, only the normal profit from manufacture will be taxable in the Netherlands. In order to ascertain this normal profit, account is taken of the price which would have been paid to an independent Netherlands enterprise if, instead of having the articles sold made in its own establishments, the foreign concern had ordered them from such enterprise. In fixing the price, consideration will be given to the particular reasons which led the enterprise to establish its factories in the Netherlands. The price thus fixed will be higher according as these reasons are stronger.

3. *Processing Establishments.*

The statements in the last paragraph concerning manufacturing establishments also apply when a foreign enterprise has establishments in the Netherlands which merely treat materials produced abroad destined for further processing or sale there.

4. *Buying Establishments.*

If a foreign enterprise has an establishment in the Netherlands whose business it is to make purchases, it is liable to tax on its presumed profits.

The gross profit therefrom is generally computed as if the buying establishment were a separate enterprise. The amount will vary according to the case and, in particular, according to the commercial skill which the operations demand.

In other cases the net profit may be ascertained direct by the use of a purely empirical method ; a certain percentage representing net profit is applied to the purchase price of each article. In this case, therefore, contrary to what happens when the above-mentioned method is employed, there is no need to deduct the expenses of the buying establishment from the profit obtained.²

¹ The decision of the Minister of Finance of November 18th, 1920, No. 15, B., No. 3028, Vol. VIII, page 322, deals with such a method.

² The decision of the Minister of Finance, dated October 31st, 1929, No. 36, B., No. 4803, Vol. XIII, page 7, deals with such cases.

5. *Research or Statistical Establishments, Display Rooms, etc.*

The fact that an enterprise possesses a research or other establishment in the Netherlands which does not directly engage in any profit-making transactions is not generally to be regarded as equivalent to the carrying-on of business in the country.

Tax, however, is imposed if these establishments are engaged in such operations that, without the establishment, the enterprise on which it depends would have to resort to the services of others. An enterprise which maintains a publicity office in the Netherlands would in all probability be liable up to the amount corresponding to the expense which the existence of such an office saves it.

(b) BANKING ENTERPRISES.¹

The following remarks do not apply to the central banks of issue in the colonies or abroad, which are exempt from Netherlands taxes on income and property, even if part of their business is conducted in the Netherlands (Income Tax Law, Article 36, and Property Tax Law, Article 9 (5)).²

The question of allocation must be discussed separately for income tax and for property tax. In either case, however, if a bank has several branches either in the Netherlands or abroad, account is taken only of the results common to all the branches in the same country, without distinguishing one from another; that is to say, the different branches in one country are treated as if they were a single branch.

Income Tax.

Profits from purchase, sale or other negotiations effected in connection with bills of exchange, securities, etc., by the enterprise on its own account are taxable against the branch or establishment initiating the operation from which the profit was derived.

Profits entered in the accounts as accruing from bills and securities are ascribed to the establishment among whose assets the securities are included at the time the inventory is made, provided, however, that that establishment is empowered to effect their sale.

Amounts withheld on operations made for the account of others must be regarded as part of the profit of the country in which the operation yielding the commission was effected. Profits from loans and advances of capital — that is, generally speaking, interest — should be regarded as having been realised in the countries where the capital was invested or lent, and losses on investments, loans, etc., as having been incurred in the country where the loans were made.

Of the interest paid by the branch itself, only that accruing to third parties may be deducted from its profits, and a branch may not deduct interest which it owes to the rest of the enterprise to which it belongs. Accordingly, since all the resources of a bank are pooled, it is very important to determine what part of the funds used by a branch for loans and investment comes from loans made by third parties and what part from sums advanced to it by another part of the enterprise. This question will be dealt with in connection with the apportionment of liabilities for purposes of property tax.

Although interest paid by a branch may only be deducted to its actual amount — that is, computed at the rate in force in the country where the money was borrowed — the part of general overhead expenses incurred in the country from which the money was borrowed should be added to it. For the general overhead expenses (rent, wages, etc.) incurred in that country have contributed to draw to the enterprise the resources of which it disposes.

¹ The explanations which follow are based on the decision of the Minister of Finance of May 7th, 1930, No. 44. B., No. 4904, Vol. XIII, page 156. It should be noted that this resolution is but an instruction given to the officials of the administration.

² See Note 3 on page 355.

By way of exception, however, the profits from investment interest may possibly not be ascribed altogether to the country where the money was invested. This happens when the rate of interest in the country from which the invested resources were obtained is permanently lower than the rate in the other country, or when a bank has been able to borrow money in another country at a much cheaper rate than the normal, because it secures for the public certain advantages at little or no expense or renders it certain services ; and the gain derived from the fact that the bank has thus been able to borrow on more favourable terms than usual is ascribed, less the cost of the services rendered to the bank's customers, to the country from which the resources employed were obtained.

Property Taxes.

For purposes of property taxes, the apportionment of assets is a simple matter. All fixed assets (buildings, plant, equipment, investments, long-term debts, holdings in other enterprises, etc.) are ascribed to the country where they are actually situated or where is situated the establishment from which they are administered. The enterprise's other assets (bills, advances, miscellaneous accounts, debts of all sorts, cash) are localised in the country where they are, or, according to the ordinary rules of accountancy, ought to be, administered. If these assets cannot be said to belong to one branch more than to another, they are allocated to the chief establishment.

The apportionment of liabilities is more complicated. Two cases must be distinguished :

First, the case in which an establishment receives funds and capital direct from its customers and third parties in such quantity that it can conduct its operations without recourse to the enterprise's own working capital or to advances made to it by other establishments. In this case, the liabilities to be deducted from the assets of the establishment in question are obtained simply by adding together all the debts and obligations of the establishment towards third parties, subject to the restriction that their total amount is diminished by the sums which the establishment has placed at the disposal of the enterprise's establishments in other countries.

The second case is that of establishments which owe money to the principal establishment or to other establishments depending on the same bank — that is, establishments which, not themselves receiving sufficient capital from their customers or from third parties, have to obtain the resources necessary for their business from the principal establishment or other establishments of the same bank coming under the first case above. These resources consist either of working capital made up out of the enterprise's own capital or of local surpluses of capital and funds from outside sources — *i.e.*, from third parties.

The former resources, being part of the enterprise's own capital, can obviously not be deducted from the assets of the particular establishment.

The treatment of the latter resources differs, as they represent a part of the liabilities of the enterprise itself to third parties, the proceeds of which were devoted to the branch whose resources would otherwise have been insufficient. But the total resources of a bank are pooled, and out of those which have been placed, as stated above, at the disposal of a particular establishment, it is impossible to distinguish between the part obtained by drawing on the bank's own capital and the other part which is made up of capital received from third parties (that is, excess of working capital received from outside and placed at the disposal of the establishment concerned by other establishments of the same enterprise), which represents a deductible liability. Accordingly, out of the resources placed at the disposal of a particular establishment by other establishments of the same bank (establishments, of course, which are situated as in the first case above), the part making up the deductible liability is obtained by ascertaining the ratio between the surpluses of working capital obtained from third parties by any of the establishments of the enterprise in question, on the one hand, and the same total plus the gross amount of the enterprise's own resources used in the conduct of its business, on the other hand. That ratio is then applied to the funds furnished to the establishment by the rest of the enterprise. Expressed algebraically, the rule is as follows :

$$\frac{A}{A+B} = \frac{l}{r} \text{ or } l = r \frac{A}{A+B}$$

Here l = the deductible liability to be determined ; A = the total local surpluses of working capital received from outside ; B = the gross amount of the enterprise's own resources used in the business of the whole enterprise — that is, the working capital taken from the bank's own capital and reserves ; r = the establishment's liabilities towards the rest of the enterprise, less the value of that establishment's capital assets.

In other words, the deductible liability to be determined (l) is to the current liabilities of the particular establishment towards the rest of the enterprise, or, if preferred, towards the resources furnished to it by the latter (after deducting the capital assets of the establishment) (r), as the total local surpluses of working capital received from outside (A) are to the sum of these surpluses and the gross total of the enterprise's own resources used in its business — *i.e.*, to the working capital taken from the bank's own capital and reserves. This ratio can, of course, be expressed in another form, which is more convenient for immediately determining the deductible liability : l is equal to the product of r and A divided by the sum of A and B .

(c) INSURANCE COMPANIES.

Income Taxes.

Before we consider the system of allocation applicable to insurance companies in the case of income taxes, we must make two preliminary observations : in the first place, profits are computed on the basis of premiums and life annuity capital received exclusively from persons whose fiscal domicile is in the Netherlands. It does not matter where the premiums or capital are paid, and the other circumstances attending the conclusion of annuity and insurance policy contracts are also immaterial ; secondly, under Articles 46 and 49 of the Income Tax Law, the tax return has to be made, not by the insurance enterprise itself, but by its representatives in the Netherlands, and there are as many assessments as there are agents or representatives of the enterprise in the country. If, however, the general management of the enterprise in the Netherlands is entrusted to one of these representatives or agents, it is he alone who has to make the return, and there will be a single assessment. In any case, the assessments are always fixed by the same inspector.

The normal system of allocation is that described in the first paragraph of Article 29 of the Law. The net taxable sum is obtained directly by applying a coefficient of 10 per cent to the net total of premiums and capital sums received from insured persons established or living in the Netherlands during the business year preceding the date of assessment. To obtain this net total, the gross premiums and capital are reduced by brokerage, commission and other allowances granted to representatives or to third parties. It should be noted that this fixed 10 per cent is the only sum on which the company is taxable on account of the carrying-on of business in the Netherlands. For purposes of tax assessment no account need therefore be taken of factors such as rental value of the enterprise's offices, the rent of premises in the Netherlands which the enterprise may have let to others (to the extent that these rents are part of commercial profits) nor of profits from the sale of real estate or other assets making up its business capital.

Under paragraph 2 of the same Article 29, insurance companies may ask to be taxed, not by the coefficient method, but by the method of fractional apportionment. In this case, the taxable profits are computed by applying to the enterprise's total net profits the ratio between gross premiums and capital received during the previous business year from insured persons residing or established in the Netherlands and the gross total of all premiums and capital received during that year. In such cases, the taxable enterprise must supply all the data necessary for the application of this method accompanied by documentary evidence in support.

Property Taxes.

It should be noted that, in the case of property taxes (unlike income taxes), the return to the fiscal administration has to be made by the company itself and not by its representatives ; and a single assessment is made for the whole Kingdom.

For purposes of property taxes there are no legal provisions specifying how the assets and liabilities of insurance companies are to be allocated, and the administration follows the directions given to it in two decisions by the Minister of Finance, dated August 30th, 1928, No. 75, B., No. 4558, Vol. XII, page 227, and May 8th, 1931, No. 96, B., No. 5145, Vol. XIII, page 582.

The first of these decisions is based upon the principle that, normally, insurance business outside the country in which the head office is situated is conducted by agents who are not in the company's service, but who have been entrusted with a certain restricted mission. In the case therefore of enterprises having their head office abroad, a minimum of assets and liabilities is to be ascribed to the Netherlands. For this reason, apart from real estate situated in the country and debts secured on such estate, which are always taxable (Article 9 *bis* of the Property Tax Law, paragraphs 1, Nos. 1 and 2), only the assets placed at the disposal of the agency and the corresponding liability need be considered. In the case of life-insurance companies, these assets will, among others, consist of :

Securities deposited in the Netherlands to guarantee the obligations incumbent upon insurance companies in regard to death duties under the Law of May 23rd, 1917 (*Staatsblad*, No. 36) (this guarantee is about 25,000 florins) ;

Loans which the enterprise may have granted on policies which the " Law on life-insurance enterprises " regards as Netherlands policies ;

Sums due to the enterprise in the form of premiums owing or paid in advance by insured persons to agents, in so far as these premiums relate to Netherlands policies within the restricted meaning given above ;

Furniture and equipment used by Netherlands agents, if they are the property of the enterprise.

Deductible debts include :

The mathematical reserves on Netherlands policies (see above) ;

Payments due to insured persons on these policies ; and

Any sums due to agents and relating to these policies.

The second ministerial decision providing for the use of the method of fractional apportionment in assessing to property tax was given in the special case of a company which had a very important branch in the Netherlands and understood the idea of Netherlands risks in a wider sense than did the " Law on life-insurance enterprises ". Hence, the company had invested quite a large proportion of its assets in real estate situated in the Netherlands or in mortgages secured on such estate.

Under fractional apportionment there is a separate computation of the assets and liabilities which are to be regarded as Netherlands assets and liabilities.

Netherlands assets are obtained by applying to the total assets of the enterprise the ratio between the mathematical reserves relating to policies which the enterprise regards as Dutch and the total mathematical reserves relating to all policies concluded by the enterprise. But if the result of this operation is smaller than the total value of the enterprise's real estate in the Netherlands and the mortgages (secured on that estate in the Netherlands), this latter sum is considered to represent the Netherlands assets.

Netherlands liabilities are calculated, *mutatis mutandis*, in the same way : the total liabilities of the enterprise are taken and to them is applied the ratio between the mathematical reserves relating to Netherlands policies and total mathematical reserves. The result gives the Netherlands liabilities, but if the figure is below the total mortgage debts on real estate owned by the company in the Netherlands, the latter amount is taken as the Netherlands liabilities.

These assets and liabilities having been thus determined, the difference between them gives the taxable sum.

*(d) TRANSPORT ENTERPRISES.**Maritime and River Transport.*

International shipping — *i.e.*, shipping between two places, one in the Netherlands and one in a foreign country — is not liable to income taxes.¹ But this is not the case with purely internal transport. There are no legal provisions nor even administrative rules for the taxation of an enterprise which is engaged in both international and internal transport, but it might be said that the taxable profits would be obtained by deducting from the receipts derived from internal transport a share of total costs which correspond to the ratio between internal transport receipts and the receipts from all transport.

Further, owing to the choice of measures taken to avoid double taxation, even internal shipping may sometimes escape liability to income tax. Netherlands maritime and river transport enterprises being exempt from income tax in the United States, all citizens of the United States (and all legal entities incorporated in that country) would be exempt if they are engaged in internal shipping in the Netherlands under the American flag. This special regime is based on the Royal Decree of October 1st, 1926 (*Staatsblad*, No. 37), and on the Law of June 14th, 1930 (*Staatsblad*, No. 244).

As regards property taxes, the fleet of a foreign enterprise used in international shipping is not regarded as constituting property devoted to business activities in the Netherlands. Only the enterprise's real estate and fixed plant in the Netherlands will be taxed, after deducting any mortgage debts secured on such property.

Railway Transport.

No special provisions are required for allocating the profits of railway and tramway enterprises whose Netherlands lines do not cross the frontier, and therefore no such provisions exist. On the other hand, enterprises whose lines extend on both sides of the frontier are governed by the provisions of Article 28 of the Income Tax Law. Briefly, this article prescribes that the taxable income of such enterprises in the Netherlands shall be determined by deducting from half the gross receipts of the Netherlands lines for the previous business year a sum equivalent to 4 per cent of the cost of primary installation. In the case of a section of line, gross receipts are, if necessary, calculated on the basis of the ratio between the length of line situated in the Netherlands and the length of the whole railway. If the line has been operated for only part of the previous business year, the sum to be deducted as interest on cost of primary installation is proportionately reduced. Foreign railways whose lines only cross the frontier as far as the first Netherlands station are, subject to reciprocity, exempt from income tax. Since international railways and tramways are thus assessed for tax empirically, no occasion arises to increase the amounts for which they are assessed on account of the rental value of premises which they may possess in connection with the part of the exploitation which extends into the Netherlands. These provisions apply, of course, only to income tax.

For purposes of property taxes there are no special provisions for these enterprises.

Road Transport.

The Income Tax Law contains no special provisions regarding the allocation of the profits of road transport enterprises, and the same is true in regard to the Property Tax Law. For purposes of the latter, however, vehicles are regarded as belonging to the country where they are garaged.

¹ Income Tax Law, Article 3. This article also exempts the staff of all means of transport engaged in international traffic, if they are resident abroad.

Air Transport.

There are no special provisions for determining the income of aviation enterprises. It seems, however, that if the problem of their taxation were to arise (that is, if they earned profits), it would correspond to the spirit (but not to the letter) of Article 3 to treat them in the same way as maritime transport enterprises.

(e) LIGHT AND GAS COMPANIES, TELEGRAPH AND TELEPHONE COMPANIES AND MINING ENTERPRISES.

There is no special system for apportioning the profits of any of these enterprises. Accordingly, unless the taxpayer and the administration agree that the method of fractional apportionment shall be employed, Netherlands profits and capital will be computed either on the basis of the separate accounts or by some more or less empirical method.

B. NATIONAL ENTERPRISES WITH BRANCHES OR SUBSIDIARIES ABROAD.

I. GENERAL METHODS OF ALLOCATION.

(a) TAX ON DIVIDENDS AND "TANTIÈMES".

The allocation of profits arises in connection with this tax, for, as we know, that part of the taxable distributions of share companies which corresponds to the foreign profits of those companies is only liable to tax in respect of one-third of its amount. Articles 27 and 28 of the law on the tax on dividends and *tantièmes*, which lay down the principle of this exemption, prescribe that colonial and foreign profits as well as the total profits shall be computed in accordance with Articles 7, 10 and 11 of the Income Tax Law. But, as these articles do not themselves supply any criterion for determining when profits are national and when they are foreign, they must be construed in the light of legal doctrine and jurisprudence relating to the "carrying-on of business abroad." ¹

Among the provisions in these articles, special mention must be made of paragraph 1 of Article 10, under which shares in profits distributed to an enterprise's staff or to third parties (provided, of course, these shares do not constitute the remuneration of the enterprise's own capital) are regarded as deductible liabilities. Hence, although we are here dealing with the tax on dividends and *tantièmes*, and although percentages and other remuneration paid to the company's staff are in principle taxable, the amount of these percentages and this remuneration will have to be deducted from the foreign profits as well as the corresponding amount from the total profits. On the other hand, as the law on dividends and *tantièmes* tax in principle exempts Netherlands dividends received by the company liable to this tax from other companies, and as the law only taxes foreign dividends redistributed by the company to the extent of one-third, all of these dividends must be regarded as accruing to the Netherlands part of the enterprise; as otherwise the result would be to increase unduly the two-thirds deduction allowed on distributions of profits which the enterprise has earned by its activities in foreign countries or overseas territories.

To conclude this account of the general rules of apportionment, the allocation of distributions in the ratio of foreign profits to total profits applies only to *taxable* distributions — that is, to the amount distributed *after* applying exemptions, but *before* applying the deductions against internal and international double taxation. ²

¹ See, *mutatis mutandis*, what has been said on pages 354 and 355 in connection with the "carrying-on of business in the Netherlands".

² See pages 337 and 338.

A special question of some importance concerns the case of an enterprise which does business in the Netherlands and in two other countries, when business in one country results in a loss and business elsewhere shows a profit.

The Supreme Court has pronounced on this question (Judgment of June 25th, 1928, B., No. 4301, Vol. XI; page 532) and has decided that the sum entitled to the two-thirds deduction shall be determined by calculating the ratio between the business results in all foreign countries (including countries where there were no profits but losses) and the total results of the enterprise's business in the Netherlands and in foreign countries (including those where there were no profits but losses).

Although this jurisprudence seems to us open to serious question, we have no space here to enter upon a controversy, which, however, would not be out of place. Let it only be said that it would appear to be in conformity with the spirit and letter of the law to ignore in both terms of the ratio countries in which the enterprise sustained a loss.

(b) INCOME TAX.

The problem of allocation again arises in connection with national enterprises liable to income tax, their foreign income being, as we have already said, under certain conditions tax-free.

The foreign profits of national enterprises liable to income tax on foreign business are allocated in principle according to the same rules as those governing foreign enterprises doing business in the Netherlands, subject to the fact that the law does not impose upon insurance companies, and railway and tramway enterprises regarded as national, the empirical or fractional apportionment methods *applicable to foreign enterprises*.

If an enterprise's assets include shares in a foreign share company, the dividends from these shares are ascribed to the country where the enterprise has its real centre of business, normally, to the Netherlands; directors' percentages and other remuneration distributed in other companies are regarded as earned in the country where the functions to which they correspond were discharged.

The special question examined in connection with the tax on dividends and *tantièmes* also arises in regard to income tax. It referred, as will be remembered, to the case of an enterprise doing business in the Netherlands and in two foreign countries and incurring a loss in one country while realising profits in the others. The solution in this case is as follows:

Losses sustained in one foreign country have no influence on the profits earned in another; that is to say, that in fact the loss incurred in a foreign country will be deducted from the profits earned in the Netherlands. For the enterprise will be, on the one hand, taxed on its Netherlands profits after deducting the loss incurred abroad and, on the other hand, will be exempt from tax in respect of the profit realised in the other foreign country (if, of course, the requisite legal conditions are fulfilled in that country).

Further, if an enterprise has in one year incurred a loss abroad, that loss is not specially deducted from its foreign profits in the following year. It might happen that as the result of very heavy losses abroad in one year, the taxpayer was liable to no tax at all in the Netherlands, his loss absorbing the whole of his other income. This will not prevent his being exempt from tax the following year in respect of all the profits he earns abroad.

(c) PROPERTY TAXES.

When a national enterprise liable to property tax does business abroad, the same rules of apportionment are applied as in the case of foreign enterprises. Shares owned by the enterprise in subsidiary companies must be ascribed to the place where the enterprise has its real centre of business — that is, normally, to the Netherlands.

If the enterprise operates in more than two countries, and if in one of them the liabilities exceed

he assets, the former are deducted, not from the assets in another country, but from the enterprise's assets in the Netherlands.

II. ALLOCATION OF PROFIT TO REAL CENTRE OF MANAGEMENT WITHIN THE COUNTRY.

With regard to national enterprises, there are no special provisions aiming at the attribution of a part of the profits to branches outside the Netherlands to the real centre of management situated in the Kingdom. The rules set forth on pages 366 *et seq.* apply, *mutatis mutandis*.

The tax on dividends and *tantièmes* being levied, however, on a third of the distributions derived from foreign or colonial profits, the result is more or less the same as if a third of the foreign or colonial profits is ascribed to the centre of management of the company.

C. HOLDING COMPANIES.

The rule stated on page 367 in connection with allocation between parent and subsidiary applies also to foreign holding companies that control Netherlands enterprises.

As regards Netherlands holding companies with foreign subsidiaries, we must refer to what was said on pages II, 360 and 361.

Annex.
—TABLE OF TARIFFS.
—

I. LAND TAX.

(a) Ordinary tax :

On buildings ¹ : 4.86 per cent of the " cadastral " income.

On lands ² : 6 per cent of the " cadastral " income.

(b) Additional taxes :

On behalf of the Loan Fund : 20 per cent of the ordinary tax. ³

On behalf of the province : variable ; maximum 50 per cent of the ordinary tax.

On behalf of the commune : variable ; maximum 80 per cent of the ordinary tax for buildings and 20 per cent of the ordinary tax for lands.

II. TAX ON DIVIDENDS AND PERCENTAGES.

(a) Ordinary tax ⁴ :

5 per cent of the actual amount of the taxable distributions and fees.

(b) Additional taxes :

On behalf of the Loan Fund : 33 per cent of the basic tax.

On behalf of the commune ⁵ : 48 per cent of the basic tax.

¹ Article 1 of the Law of July 14th, 1907 (*Staatsblad*, No. 203).

² Law of December 31st, 1892 (*Staatsblad*, No. 315).

³ From January 1st, 1933, additional tax is levied only on buildings.

⁴ Law of January 4th, 1918 (*Staatsblad*, No. 4, Article 10).

⁵ Or of the communes in which the enterprise operates.

III. INCOME TAX. ¹

(a) Ordinary tax applicable to taxpayers other than legal entities.

Income (In florins)		Amount of tax corresponding to the first figure of the "income" column (In florins)	Rate of tax applicable to the slices ² of income comprised between the two figures of the "income" column (Per cent)
Between	And		
0	750	0.00	0.0
750	1,000	0.00	1.2
1,000	1,150	3.00	1.6
1,150	1,200	5.40	3.2
1,200	1,600	7.00	2.0
1,600	2,000	15.00	2.4
2,000	4,000	24.60	2.8
4,000	7,000	80.60	3.2
7,000	10,000	176.60	3.7
10,000	15,000	287.60	4.2
15,000	20,000	497.60	5.0
20,000	25,000	747.60	5.8
25,000	30,000	1,037.60	6.6
30,000	35,000	1,367.60	7.4
35,000	40,000	1,737.60	8.3
40,000	45,000	2,152.60	9.3
45,000	50,000	2,617.60	10.3
50,000	60,000	3,132.60	11.3
60,000	70,000	4,262.60	12.3
70,000	85,000	5,492.60	13.3
85,000 and over		7,487.60	13.5

¹ Law of December 19th, 1914 (*Staatsblad*, No. 563, Article 37).² Up to 1,600 florins, the slices are of 50 florins, and above, of 100 florins. All fractions of a slice are omitted in the calculation.

(b) Deduction to be made on the net income on account of the taxpayers' dependents in accordance with Article 38 of the Income Tax Law of December 14th, 1914 (*Staatsblad*, No. 563).

Amount of net income (In florins)		Amount of the deduction to be made on account of each child (In florins)	
Between	And	If the number of children does not exceed four	If the number of children exceeds four
0	1,400	100	125.00
1,400	1,500	110	137.50
1,500	1,600	120	150.00
1,600	1,700	130	162.50
1,700	1,800	140	175.00
1,800	1,900	150	187.50
1,900	2,000	160	200.00
2,000	2,300	170	212.50
2,300	2,600	180	225.00
2,600	3,000	190	237.50
3,000 and over		200	250.00

(c) Ordinary tax applicable to Dutch foundations and to foreign and colonial legal entities :
6.40 florins for each 100 florins comprised in the taxable amount.

(d) Additional taxes :

On behalf of the Loan Fund : 20 per cent of the ordinary tax.

On behalf of the province¹ : variable with the locality ; maximum 40 per cent of the ordinary tax.

¹ Payable only by individuals domiciled in the Kingdom.

III. INCOME TAX. ¹

(a) Ordinary tax applicable to taxpayers other than legal entities.

Income (In florins)		Amount of tax corresponding to the first figure of the "income" column (In florins)	Rate of tax applicable to the slices ² of income comprised between the two figures of the "income" column (Per cent)
Between	And		
0	750	0.00	0.0
750	1,000	0.00	1.2
1,000	1,150	3.00	1.6
1,150	1,200	5.40	3.2
1,200	1,600	7.00	2.0
1,600	2,000	15.00	2.4
2,000	4,000	24.60	2.8
4,000	7,000	80.60	3.2
7,000	10,000	176.60	3.7
10,000	15,000	287.60	4.2
15,000	20,000	497.60	5.0
20,000	25,000	747.60	5.8
25,000	30,000	1,037.60	6.6
30,000	35,000	1,367.60	7.4
35,000	40,000	1,737.60	8.3
40,000	45,000	2,152.60	9.3
45,000	50,000	2,617.60	10.3
50,000	60,000	3,132.60	11.3
60,000	70,000	4,262.60	12.3
70,000	85,000	5,492.60	13.3
85,000 and over		7,487.60	13.5

¹ Law of December 19th, 1914 (*Staatsblad*, No. 563, Article 37).² Up to 1,600 florins, the slices are of 50 florins, and above, of 100 florins. All fractions of a slice are omitted in the calculation.

(b) Deduction to be made on the net income on account of the taxpayers' dependents in accordance with Article 38 of the Income Tax Law of December 14th, 1914 (*Staatsblad*, No. 563).

Amount of net income (In florins)		Amount of the deduction to be made on account of each child (In florins)	
Between	And	If the number of children does not exceed four	If the number of children exceeds four
0	1,400	100	125.00
1,400	1,500	110	137.50
1,500	1,600	120	150.00
1,600	1,700	130	162.50
1,700	1,800	140	175.00
1,800	1,900	150	187.50
1,900	2,000	160	200.00
2,000	2,300	170	212.50
2,300	2,600	180	225.00
2,600	3,000	190	237.50
3,000 and over		200	250.00

(c) Ordinary tax applicable to Dutch foundations and to foreign and colonial legal entities :
6.40 florins for each 100 florins comprised in the taxable amount.

(d) Additional taxes :

On behalf of the Loan Fund : 20 per cent of the ordinary tax.

On behalf of the province¹ : variable with the locality ; maximum 40 per cent of the ordinary tax.

¹ Payable only by individuals domiciled in the Kingdom.

IV. TAX FOR THE COMMUNAL FUND. ¹

(a) Ordinary tax applicable to taxpayers other than foreign legal entities.

Income (In florins)		Amount of tax corresponding to the first figure of the income column (In florins)	Rate of tax applicable to the slices ² of income comprised between the two figures of the "income" column (Per cent)
Between	And		
0	750 (850) ³	0	0
750 (850)	1,500 (1,300)	0	2
1,500 (1,300)	4,000	15 (9)	3
4,000	7,000	90	4
10,000 and over	10,000	210	5
—	—	360	6

(b) Ordinary tax applicable to foreign legal entities :

Two florins for each 100 florins included in the taxable amount.

(c) Additional taxes :

On behalf of the commune, ⁴ variable according to the locality ; maxima 80 and 100 per cent of the ordinary tax.V. PROPERTY TAX. ⁵

(a) Ordinary tax :

Normal rate :

1 florin for each whole thousand florins of the taxable property.

Special rate applicable when the taxable property does not exceed 30,000 florins :

2 florins for each whole 1,000 florins remaining after deduction of 15,000 florins from the taxable property.

(b) Additional taxes :

On behalf of the Loan Fund : 55 per cent of the ordinary tax.

On behalf of the Communal Fund ⁶ : 50 per cent of the ordinary tax.On behalf of the province ⁶ : variable ; maximum 40 per cent of the ordinary tax.On behalf of the commune ⁷ : variable ; maximum 50 per cent of the ordinary tax.¹ Articles 15 and 17 of the Law of July 15th, 1929 (*Staatsblad*, No. 388).² Up to 1,600 florins, the slices are of 50 florins, and above of 100 florins. All fractions of a slice are omitted in the calculation.³ The figures in parentheses are those which apply instead of the ordinary figures next to which they stand in the case of taxpayers living in the first-class parts of the communes of Amsterdam, Rotterdam and The Hague.⁴ Payable only by individuals who have their domicile in a specified commune of the Kingdom.⁵ Article 10 of the Law of September 27th, 1892 (*Staatsblad*, No. 223).⁶ Payable only by individuals domiciled within the Kingdom.⁷ Payable only by individuals having a domicile in a specified commune of the Kingdom.

VI. DEFENCE TAX NO. I. ¹

Amount of taxable property (In thousands of florins)		Amount of tax corresponding to the first figures of the "taxable property" column (In florins)	Rate of tax applicable to the slice of the taxable property ² which is included between the two figures of the "taxable property" column (Per thousand)
Between	And		
0	50	0	0.00
50	100	0	0.30
100	150	15	0.60
150	200	45	1.00
200	300	95	1.40
300	400	235	1.80
400	500	415	2.20
500	750	635	2.60
750	1,000	1,285	3.00
1,000	1,250	2,035	3.50
1,250	1,500	2,910	4.00
1,500	2,000	3,910	4.50
2,000	3,000	6,160	5.00
3,000	4,000	11,160	5.50
4,000	5,000	16,660	6.00
5,000	6,000	22,660	6.50
6,000	7,000	29,160	7.00
7,000	8,000	36,160	7.50
8,000	9,000	43,660	8.00
9,000	9,936	51,660	8.50
9,936 and over		6‰ of the total property	

¹ Article 3 of the Law of March 16th, 1928 (*Staatsblad*, No. 66).

² In the calculation, figures are taken to the nearest thousand below, hundreds, tens and units being omitted.

ROUMANIA

BY

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PART I. — GENERAL DESCRIPTION OF INCOME-TAX SYSTEM.¹

The income-tax is made up of six schedular or "elementary" taxes, objective and proportional, to which must be added the "total" tax on the whole income, which is a personal and graduated tax (Law for Unification of Direct Contributions and Introduction of the Tax on Total Income, *Official Monitor*, No. 235, of February 23rd, 1923). The yield of these direct taxes represents a little more than one-quarter of budget revenue.²

The schedular taxes are levied upon individuals and legal entities, irrespective of nationality or domicile.

Partnerships (*sociétés en nom collectif* and *sociétés en commandite simple*) are subject to each of the schedular taxes in the same way as individuals. But, for purposes of the tax on total income, the share of each partner (whether distributed or not) is taxed separately in the partner's name.

Schedular taxes are objective in character but the law has provided for certain exceptions to this rule, either on the ground of domicile or of the personal circumstances of the taxpayer.

I. GRADUATED TAX ON TOTAL INCOME.

The graduated tax on total income, which is levied upon individuals only, and not on companies and corporations, is payable by all persons habitually resident in Roumania, whatever their nationality. A foreigner is "habitually resident" in Roumania if he lives there for more than six months in all in a calendar year.

Roumanians domiciled abroad, however, have to pay the Roumanian tax on total income in respect of the whole of their income.

Foreigners not residing in Roumania are liable to the tax on total income on account of all the income, other than income from securities, they derive from the country. In that case the tax on total income consists in a surtax amounting to 50 per cent of the schedular taxes due on the taxable income. But the tax is not increased by additional centimes.

¹ Legislation in force on June 30th, 1933.

² The following is a list of direct taxes showing their relative importance :

	Average percentages 1926 to 1930
1. Tax on agricultural income	15.26
2. Tax on income from buildings	8.78
3. Tax on income from securities	14.03
4. Tax on commercial and industrial income	18.99
5. Tax on salaries and wages	23.55
6. Tax on income from professions and occupations not subject to other taxes	3.37
7. Graduated tax on total income	16.02
	100.00

Direct taxes have steadily gained in importance over indirect taxes, their yield increasing between 1926 and 1930 from 4,900 to 9,078 million lei — *i.e.*, from 16.3 per cent to 26.1 per cent of the total budget revenue. Of an average total revenue of 33,439 million lei from 1926 to 1930, direct and indirect taxes represent 59.7 per cent, the balance consisting of revenue from stamp and registration duties, monopolies and other miscellaneous sources.

The tax is assessed upon a return which every taxpayer has to make during January of each year for each category of income he has enjoyed during the preceding year, except agricultural income; the return regarding which has to be made at the beginning of the general census period, and income from buildings, the return concerning which is made whenever there is a change in the income amounting to at least 25 per cent of the taxable income.

In addition, there exists a number of provisions, recently amended by the law published in the *Official Monitor*, No. 237 of October 10th, 1932, authorising the deduction from the amount, subject to the tax on total income, of certain expenses which are not allowed in connection with the elementary taxes, providing abatements on account of dependents and fixing the taxable minima. Further, the law provides for the determination of the taxable income by means of indices—*i.e.*, the rental value of the house occupied by the taxpayer, the number of servants, the number of automobiles, and, also, for persons deriving an income exceeding 40,000 lei, the amount of their personal expenses.

II. TAX ON AGRICULTURAL INCOME.

According to Articles 3 to 12 of the Law of February 23rd, 1923, income from agricultural landed property in Roumania or property assimilated thereto, such as arable land, pasturage, orchards, ponds, market and other gardens, is subject to the agricultural tax. The tax is paid annually by the owner,¹ usufructuary or any other beneficiary of the income.

When such property is worked by farmers, they are subject to the commercial and industrial tax, notwithstanding the fact that the owner remains subject to the agricultural tax.

Forests are subject to this tax only when income derived from them is other than income from felling. If they are felled either by the owner or some other person, they are liable to both agricultural tax and to commercial tax (Law of February 23rd, 1923, Articles 6 and 30).

Land leased for mining is only subject to this tax in respect of agricultural income derived from above ground, but taxation ceases directly when this income disappears by reason of the exploitation of the subsoil. The income of the conceding party is taxed as personal income, that of the concessionary as commercial income (Law of February 23rd, 1923, Article 7 and Article 23, paragraph 6).

The taxable income is the gross income as determined by census committees every five years.

The taxable income is ascertained by taking as a basis the average rental value in the commune according to the leases contracted during the four preceding years, the average production value per hectare for the same period or the average sale price of properties for the same four years. In this case, the income is estimated at 5 per cent of the average sale price. The owner is required to furnish the committee with a return and all necessary evidence.

Taxpayers whose total incomes are below the minimum exempted from the tax on total income and whose total agricultural income does not amount to 2,000 lei are granted a 25 per cent reduction. The tax may also be reduced by 10 to 20 per cent on account of dependents (Article 68 of the Law).

The tax is reduced by an amount corresponding to the tax levied on interest on any mortgage or preferred debts by which the property in question is encumbered. Deduction is also made in the event of a total loss of harvest, if not insured (Article 69).

Property recently planted with fruit-trees, as also property restored to cultivation after having been devastated during the war, is exempted during the five years following its replantation with fruit-trees (Article 8).

¹ In virtue of constitutional provisions, only Roumanian nationals may own rural landed property.

III. TAX ON INCOME FROM BUILDINGS.

Under Articles 13 to 21 of the Law of February 23rd, 1923, income derived from houses and from properties assimilated thereto, such as waste land, yards, depots and other uncultivated land used commercially or industrially, playgrounds, ferries, bridges, canals, as well as railways and their appurtenances are subject to the tax on income from buildings. The owner, usufructuary or any other beneficiary of the income pays the tax each year direct to the Treasury.

Income derived from the hiring of furniture in furnished houses is separately taxed as income from non-commercial occupations, except when the owner makes a business of hiring of furniture or letting houses ; in this case, the income from hiring furniture is taxed as commercial income.

Buildings belonging to persons domiciled abroad are taxed at a rate increased by 100 per cent. This applies also to buildings belonging to companies having their head office abroad, if they are used for any other purpose than that for which authorisation was granted them to do business in Roumania.

In every case the income is fixed by a census based upon the rental value as shown by the leases, if any ; otherwise by a direct assessment—*i.e.*, one based upon comparison with similar property in the same neighbourhood. As regards waste land, income may be determined on the basis of the average sale price, and in this case the rental value is considered to be 5 per cent.

To obtain the net taxable income, 20 per cent is deducted from the rental value, representing costs of administration, insurance, upkeep and depreciation (Article 16 of the Law).

As regards real estate assimilated to buildings, the rental value is the taxable net income (Article 16 of the Law).

The tax reductions are the same as for agricultural income, except that, instead of deducting the tax on interest on debts on the property, 20 per cent of the amount of this tax is first taken off, on account of the fact that the rental value has been reduced by 20 per cent before constituting a basis for taxation.

Exemption is granted in respect of public buildings or buildings allocated to some public service and producing no income, to peasants' cottages with three or fewer habitable rooms and to buildings necessary for farm work (Article 17 of the Law). New buildings of any kind enjoy temporary exemption for ten years from the time when they are first ready for use, an exemption of 75 per cent for the next five years and of 50 per cent for the succeeding five years (Article 17, as amended by the Law of March 1933).

IV. TAX ON INCOME FROM PERSONAL PROPERTY.

I. TAXPAYERS.

The tax on income from personal property (Articles 22 to 29 of the Law) is levied upon all income of this class derived from Roumanian sources and on all income derived from foreign sources by persons resident in Roumania or by companies and partnerships having their head office in the country.

Sums accruing to the partners in a limited partnership from operations of the association are subject to this tax as against the individual partner and are also subject to the commercial tax as against the association.

For the purpose of assimilating them to Roumanian companies, foreign companies with branches in Roumania are liable to this tax in respect of that part of dividends paid abroad which represents profits earned in Roumania. No tax is due, however, if no dividend has been distributed (Article 23, *ad* paragraph 48, of Instructions by the Central Fiscal Committee published in *Official Monitor*, No. 79, of April 11th, 1929).

2. TAXABLE INCOME.

Article 23 of the Law of 1923 on direct taxes gives a list, for purposes of illustration, but which does not profess to be exhaustive, of incomes subject to this tax. The list is necessary in order to explain the regime and the rate applicable to the different forms of income from personal property.

The tax is levied upon all income derived from Roumanian securities of any kind and on such income from abroad accruing to Roumanian inhabitants.

Income from the licensing of patents and from the cession of other intangible rights, as well as the royalties and interest accruing to the grantors of such rights, are subject to the tax on income from personal property, whether they are collected in kind or in cash.

Dividends, even in the form of issues of shares, and distributions of corporate reserves, are also taxable.

The interest on funds deposited in Roumanian banks by foreigners domiciled in another country are taxed at a reduced rate.

Income from invested capital (interest on bonds, mortgage, preferred, unsecured loans, etc.) accruing to banks, merchants and industrialists is not subject to the tax on income from personal property, being included among the profits of the enterprise and liable, along with other income, to the tax on commercial income.

Exemptions.

The following classes of income are exempt :

- (1) Interest on small savings not exceeding a capital sum of 10,000 lei ;
- (2) Interest on mortgage or preferred loans of institutions authorised by law to issue secured bonds or mortgage warrants ;
- (3) Interest on annuities and bonds belonging to educational or charitable institutions, if deposited with the Deposit Bank (*Caisse des dépôts et consignations*) ;
- (4) Interest and commissions paid abroad for credits in a foreign currency granted in favour of Roumanian commercial or industrial enterprises, up to 10 per cent, the excess being taxed. If these credits are not commercial or industrial, they are entitled to no exemption (Article 23, *ad* paragraph 51, of the Instructions published in *Official Monitor*, No. 245, of February 28th, 1925) ;
- (5) Interest on mortgages, the purpose of which is to guarantee credits opened abroad in a foreign currency for commercial purposes ;
- (6) Annuities paid by the State to those who have given their property to the State for educational or charitable purposes.

3. ASSESSMENT OF TAX.

The rule is that the tax is directly applied to the gross income without any previous deduction. However, an exception is made to this rule in the case of income or royalties derived from the cession of patents, copyrights, trade marks and other incorporeal rights, as well as from mining and other concessions, when the owner of such rights has invested funds of his own in buildings or plant with a view to exploiting the ceded property and when such building and plant depreciate by use.

When these conditions coexist, it is permissible to deduct from the income an amount corresponding to the depreciation of the investments. The concessionary is also entitled to deduct annually from the profits derived by him from the exploitation of such property a certain sum for amortisation. In both cases, amortisation is reckoned by dividing the capital invested by the number of years the concession lasts.

The annual amount which may be allowed for the amortisation of capital invested by the grantor of the concession in plant which does not entirely cease to exist after expiry of the contract is determined by the Taxation Committee, but may not exceed 5 per cent of the said capital (Article 27 of the Law).

If, on the other hand, the concessionary is obliged under the contract to invest in personal or real property which, after the expiry of the concession, will remain the property of the conceding party, such investments will be assessed and added to the income from the concession and will thus be taxed.

4. COLLECTION OF TAX.

In the case of Roumanian securities, the debtors are required to withhold the tax from the amount paid. If the income from foreign securities is collected through a bank in Roumania, the latter must deduct tax; otherwise the taxpayer domiciled in the country and in receipt of this income must declare it, and the tax is paid by him direct.

V. TAX ON COMMERCIAL AND INDUSTRIAL INCOME.

I. TAXPAYERS.

The tax on commercial and industrial income is levied upon the income of all individuals or corporations — irrespective of domicile or nationality — who do business constantly and habitually through a permanent establishment in Roumania (Articles 30 to 42 of the Law). The law does not require that the taxpayer shall be a merchant (*commerçant*) within the meaning of the Commercial Code.

In addition to the elementary tax, the law provides for a supplementary graduated tax.

Share companies, both Roumanian and foreign, are granted special treatment in regard to this tax (see No. 3 (b) below).

Roumanian branches of foreign enterprises, whose head office is in another country and which are not registered in Roumania in accordance with the Roumanian Commercial Code, pay this surtax at the maximum rate (Decision of the Central Fiscal Committee communicated by Order of the Ministry of Finance No. 138667 of May 30th, 1927).

2. TAXABLE INCOME.

The tax is only levied upon net national incomes derived from an association of labour and capital, whether movable or immovable. If the acts which give rise to the income are not regular and continuous, the taxpayer does not come within this schedule. The following incomes are liable to this tax :

- (1) Agricultural income and income assimilated thereto, when accruing to a farmer ;
- (2) Income from forests, mines, ponds, nursery-gardens, etc., exploited either by the owner or by some other person ;
- (3) Income from ships and boats ;
- (4) Income from commercial or industrial enterprises belonging to communes, departments or the State ;
- (5) Income from commerce and industry ;
- (6) Profits from a transport enterprise ;
- (7) Income from State securities, which are exempt under the Law of Issues, is liable to the commercial or industrial profits tax (Supreme Court (Cour de Cassation), Section III, Decision No. 834 (b), dated April 10th, 1925 ; *ad* paragraph 89 of Instructions).

3. ASSESSMENT OF TAX.

(a) *Computation of Taxable Income and Deductions.*

According to Articles 30 and 39 of the Law of February 23rd, 1923, the tax is calculated on net income which may be determined in two ways : (a) from the balance-sheet, (b) by presumption.

The second method may only be employed when there is no balance-sheet or when the balance-sheet does not tally with the books.

Even when the books are properly kept, the Assessment Committee may refuse to include certain items of expenditure which it thinks excessive or unnecessary and which thereby unjustifiably reduce the net income (Bucharest Court of Appeal, Section IV, Decision No. 15 of January 28th, 1926, and Decision No. 174 of September 20th, 1928).

Net income is found by deducting the liabilities from the assets, that is, it is equal to the difference between gross income (assets) and the expenses recognised by the law (liabilities).

The assets include the following items amongst others :

1. Merchandise is valued according to the following rules :

(a) As regards commerce, the basis taken is the purchase price, to which are added all costs until the goods are stored.

If the price at the date of the balance-sheet is lower than the purchase price, the former is taken as the basis ; if higher, the purchase price is the basis.

(b) As regards industry, raw materials are assessed as for commerce ; manufactured goods are assessed according to the cost price at the date of the balance-sheet, account being taken of the cost of the raw material and of production at the time. A rise in the value of raw materials and manufactured articles left in store is not taken into account, assessment being made according to the actual cost of production or purchase price at the time of manufacture or purchase.

2. Shares and securities. These are assessed at their value at the date when the accounts are closed, if their quotation is lower than the figure calculated in the previous balance-sheet, or at the value in the previous balance-sheet, if the prices are rising. In the case of securities bought during the year, the price taken is always the price at the date when the accounts are closed.

3. Accounts receivable — that is, all claims and sums due. They are reckoned at their face value which can only be reduced in the event of actual loss.

4. Interest : The interest accruing to banks on their deposits with other banks (which is exempt from the tax on income from personal property) is also taken into account.

5. Income from real property belonging to and used by an industrial enterprise and incapable of being used for any other purpose is also included, except where new buildings are concerned. In this case, the income from such property enjoys the same exemptions as property coming within the scope of the tax on buildings.

Liabilities — that is, deductible expenses — are composed, amongst others, of the following items (it should be noted that only the expenses relating to the taxable period are deductible and that past losses may not be carried forward) :

1. The rent for lease of real property used by the enterprise. If property belonging to the enterprise has already been taxed separately as buildings, the gross income from it must be deducted, so as to avoid double taxation.

2. The interest on borrowed capital, even when secured by a mortgage and even when it is not a fixed sum — for instance, the share of profits distributed to creditors in consideration of their loans or advances.

Interest allowed by the company itself to its own reserve funds and debited in the profit-and-loss or interest account is not included among liabilities and is therefore taxable.

3. Wages, emoluments, remuneration, shares in profits, allowances, etc., granted to officials, exclusive of any remuneration paid to the owners of, or partners in, enterprises.

The labour, production or consumption bonuses of co-operative societies are not regarded as wages and do not count among liabilities. Directors' fees, which are paid out of profits, are also not regarded as wages, and they too do not figure among liabilities.

4. The cost of raw materials bought or processed during the year.

5. The depreciation of real property and plant belonging to the enterprise : in principle this may not exceed 3 per cent per annum of the purchase price. However it may go as high as 5 per cent in the case of factories (buildings) and 15 per cent in the case of certain fixed plant (machinery).

In order that depreciation may be allowed, the property or plant must not have been taxed in any other schedule.

The amortisation of capital invested in working concessions (mining concessions or invention patents) granted for a limited time is allowed, except in the case of assets forming part of the registered capital of a company. The law does not include sinking funds created without any precise destination — for example, for " depreciation of assets ".

No allowance is granted for amortisation of investments made during the year. Any increase of value in the inventory as compared with the price in the accounts is disregarded.

6. The rent of plant and equipment which by its nature is not real property. If it belongs to the exploiter, an annual amount corresponding to the necessary depreciation may be deducted, provided it does not exceed 15 per cent of the cost price. However, in exceptional cases it may go up to 20 per cent, and for cinematographic films up to 33 per cent.

7. General overhead, including taxes, except the commercial tax.

8. Actual losses on bills or accounts receivable held for more than one business year. These are not regarded as actual losses until entered as such in the profit-and-loss account.

9. Special reserves for bad debts up to 3 per cent (and exceptionally up to 5 per cent) of the total accounts receivable of the enterprise.

As regards enterprises other than share companies, only the above deductions are permitted. But, in the case of share companies, the following deductions may also be made :

1. The statutory reserves. These may not exceed 10 per cent of profits, if their total is less than 25 per cent of the capital, and 5 per cent if their total does not exceed 50 per cent of the capital.

The mathematical reserves of insurance companies are excepted from these restrictions.

2. Income from investments made by the company which are already subject to the tax on income from personal property or to any other tax.

3. Profits intended for distribution as dividends, whether distributed or not, and this because such dividends are subject to the tax on income from personal property, which is borne by their beneficiaries.

(b) *Computation of Tax and Abatements.*

This tax is made up of two separate taxes : an elementary tax and a graduated surtax, which is called " complementary tax ".

1. The normal rate of the *elementary* (or *schedular*) *tax* is 10 per cent. This is increased by 2 per cent for enterprises engaged in banking, discount or loan operations and reduced by 2 per cent for the income of enterprises exclusively concerned with industrial or transport business.

Building enterprises, and those assimilated to them are also entitled to this reduction.

Further, the tax is not levied upon exclusively industrial or mining enterprises during the first five years of their existence, unless the profits exceed 8 per cent of the capital plus reserves ; if their profits are between 8 and 10 per cent, they enjoy a reduction of 50 per cent of the tax.

If their activities combine industry and commerce in a normal way and not accidentally, these enterprises cease to enjoy these advantages (Article 30, *ad* paragraph 73 of the Instructions). (Decision of the Central Fiscal Committee communicated by Order of the Minister of Finance No. 92700, dated April 2nd, 1928.)

In virtue of the Law of March 18th, 1933, the income subject to the elementary tax may not be inferior to a certain minimum. This minimum is determined in a different manner with regard to companies and with regard to individuals. The minimum taxable income of companies amounts to 2 per cent of their capital plus reserves for industrial companies and to 3 per cent for commercial companies, and this income is taxed at the same rate which would be applicable to the actual income, taking into account the nature of the enterprise. The tax on this minimum income may never be less than 100,000 lei if the company's capital exceeds 600 million lei, but, while normally the complementary tax is assessed, as we shall see later, only on the fraction of the income which exceeds a certain percentage of the capital of the enterprise, in this case the total amount of the minimum income is taxable.

With regard to individuals, the minimum taxable income is arrived at by multiplying by 1.5 or 2.5 the rental value of the commercial or industrial premises, according to the nature of the enterprise. The minimum income of enterprises belonging to individuals which are exclusively of an industrial nature are valued at 2 per cent of the total amount of the capital invested in the business in the form of real or personal property. In no case may the minimum tax be inferior to 18,000 lei, or in excess of 75,000 lei. The provisions relating to the minimum income apply only to taxpayers who are annually assessed, but not to petty tradesmen, who are taxed at a fixed rate according to the category in which their income is included — which category is determined every three years.

2. The surtax is assessed as follows, on the same income as is liable to the elementary tax :

(a) For an individual to be subject to the complementary tax it is necessary, in the event of his keeping books and accounts that the annual profits shown in the balance-sheet should exceed 75,000 lei, and that, when he keeps no books, his turnover should exceed 1,000,000 lei per year. In addition, for both classes of taxpayer it is necessary that the percentage of the profits to the capital employed in the enterprise should amount to at least 15 per cent. The tax rises according to a progressive tariff from 0.5 to 20 per cent. However, when accounts are kept, 10 per cent of the profits is deducted before the tax is computed.

(b) Share companies are liable to the surtax when the percentage of their profits to their capital exceeds 10 per cent. This difference of treatment is due to the fact that, in the case of companies, reserves are deducted from the profits which are subject to the elementary tax, while such deduction is not made where individuals are concerned. Further, the scale of the surtax rises from 0.5 to 25 per cent (Article 42 of the Law), the purpose of this being to restore a certain equilibrium in the burden of taxation, as the amount of the global tax which individuals are obliged to pay on their total income is materially higher than the tax paid by shareholders on the dividends which accrue to them. Account should again be taken of the privilege which is granted to corporations when they are permitted to deduct the profits allocated to reserves in the computation of the elementary tax.

The rules applied in computing the income, with a view to determining the percentage of the capital which it represents for the purpose of the complementary tax, are different from those applied in connection with the elementary tax. While for the latter the following items are deducted from the gross income :

(1) Amount of the profits which are allocated to statutory reserves ;

- (2) Sums allocated to special reserves for doubtful debts ;
- (3) Receipts derived from participations in the profits of other companies ;
- (4) Royalties from the concession of patents, trade-marks, etc. ;
- (5) Interest on loans, etc. ;
- (6) Dividends.

It is only permitted, in order to ascertain the net profits assessable to the complementary tax, to deduct from gross profits the sums included under Nos. 4 to 6 above.

The capital used as a basis for the determination of the percentage is the registered capital plus the statutory and special reserves, and the percentage is arrived at by comparing the net profit with the capital computed as above. Foreign companies which possess a branch in Roumania are taxed at the maximum rate (that is, the rate which corresponds to the maximum percentage of profits to capital), except where the capital employed by the Roumanian branch has been definitely fixed.

4. COLLECTION OF TAX.

The taxpayer makes a return in January and pays the tax quarterly, the payments for the first two quarters being based upon the previous year's tax. When the amount of tax is fixed by the authorities, compensation is made, if necessary.

VI. TAX ON SALARIES AND WAGES.

The tax on salaries and wages is levied upon the remuneration of persons living in Roumania, even if it is received for services rendered abroad, and upon that earned in Roumania by persons living abroad (Law of February 23rd, 1923, Articles 43 to 47).

The taxable income includes all net income from wages paid by public bodies or private employers, emoluments, bonuses, allowances of all kinds, shares in profits (both of directors and employees), pensions and annuities, on condition that they are continuous and regular payments.

To arrive at the net income, all expenses incurred in its acquisition (travelling expenses, etc.) should be deducted from the gross income, and, in addition, certain personal deductions may be made, as follows :

- (a) An amount of 750 lei per month, as tax-free minimum ;
- (b) The surplus, over and above twenty days' work in the month, received by manual workers employed by the day or hour ;
- (c) Premiums paid to pensions or compensation funds, as well as premiums paid in virtue of life or accident insurance policies, up to 10 per cent of the taxpayer's income.

For that part of the income which, after deduction of the principal items, does not exceed 4,000 lei per year the tax is reduced by one-half. If the taxpayer receives salaries or perquisites from more than one source, the deductions and abatements mentioned above are only made on one salary. Pensions received by men disabled in the war, by war widows and orphans are tax-free. The collection of the tax is effected by withholding at the source, except as regards the salaries received from another country, in which case a return should be made.

VII. TAX ON INCOME FROM PROFESSIONS AND OCCUPATIONS NOT SUBJECT TO OTHER TAXES.

With regard to persons residing in Roumania, all income coming within the scope of the tax on income from professions and occupations not subject to other taxes is subject to this tax, even if such income is derived from abroad.

On the contrary, persons residing abroad are subject to this tax only on account of income comprised in this schedule which is derived from Roumania (Law of February 23rd, 1923, Articles 48 to 50).

This tax resembles the tax on salaries and wages, as it is levied on income derived from labour without the association of capital, but it differs therefrom in as far as the income on which it is levied is derived from services rendered without continuity, as is the case in the liberal professions.

The income from non-commercial occupations carried on in an independent manner, as well as incomes which have not been subject to one or other of the preceding taxes, are also included in this schedule. It should, however, be noted that fixed fees and attendance fees which are granted to directors of companies and other persons assimilated to them are considered as salaries and are therefore subject to the tax on salaries and wages.

The net taxable income is arrived at by deducting from the gross income the expenses which are strictly necessary for its acquisition. The law determines for each class of taxpayer subject to this tax the amount of deductions to which they are entitled on their gross income by reason of such expenses; for instance, as regards the liberal professions, the amount which may be deducted for professional expenses is one-third of the income. Moreover, in order to alleviate the fiscal burden falling on taxpayers entering a liberal profession, the tax is reduced by two-thirds for the first three years following their entry into such profession and by one-half for the two years which follow this period.

The tax is reduced in favour of taxpayers engaged in literary, artistic or scientific work (Article 48 of the Law). With regard to the liberal professions, a minimum basis of taxation is established by the law. This minimum is computed on the basis of the rental value of the premises used for the exercise of such professions or for the residence of the taxpayers, who are classified in these categories according to the importance of the community in which they reside, and the basis for taxation is obtained by applying to this rental value a coefficient fixed in accordance with the category under which the interested party comes.

The taxpayer must file a return in January of each year and the tax is paid quarterly. Payments for the first two quarters are made on the basis of the previous year's tax. When the tax is fixed, provision is made for any necessary compensation.

PROCEDURE AND APPEALS.

As shown above, the assessment of the tax on agricultural income and on income from buildings is made by a census commission, while the assessment of the other schedular taxes and of the global tax is made by tax commissions of first instance. As regards taxes on commercial and industrial profits, on salaries and wages and on the income from non-commercial occupations or professions, a representative of each category of taxpayer is attached to this commission, to which he acts in the capacity of adviser. Taxpayers and the fiscal authorities may file an appeal against the decisions of these two commissions before the commissions of appeal, which are composed of a judge of the local court assisted by a representative of the taxpayers and a tax official. Appeal also lies against the decisions of this second jurisdiction, and in such a case the final decision is rendered either by the local civil court, if the income in litigation does not amount to 100,000 lei, or by the court of appeal if the case relates to income superior to that amount.

PART II. — METHODS OF TAXING FOREIGN AND NATIONAL ENTERPRISES.

A. FOREIGN ENTERPRISES.

1. DEFINITION AND GENERAL PRINCIPLES.

Those enterprises are foreign which are incorporated and have their registered office abroad. They are taxable in Roumania if they have a permanent establishment in that country or derive income therefrom.

The income of a foreign enterprise belonging to an individual or a partnership is taxed in the same way as the similar income of a national, except that the tax on total income is replaced by the 50 per cent surtax on income other than income from personal property.

In the case of companies, no account is taken of the general results of the enterprise's operations, and the income taxable in Roumania is the income as shown by the accounts of the Roumanian establishment.

Foreign share companies having no establishment in Roumania are only taxed if they have a depot and sell their goods in the country through an agent or representative ; they are then liable to the commercial tax (Instructions, *ad* paragraph 1 of Article 2, *Official Monitor*, No. 163, of June 26th, 1923). Partnerships and individuals doing business in the manner described above are further subject to a surtax equal to half the schedular tax, excluding the additional centimes leviable by departments and communes (Article 64 of the Law of February 23rd, 1923) ; this surtax takes the place of the tax on total income.

If the company has a permanent establishment in receipt of an income in Roumania, it is liable in respect of that income without regard to the general results of the company's total operations.

In order to avoid double taxation, share companies may deduct from their income receipts already taxed under some schedule, except income assessable to commercial or industrial tax. Such income, however, continues to be subject to the surtax on industrial and commercial income.

Individuals are liable, in addition to the schedular taxes, to the personal tax on total income, and it should be borne in mind throughout the following survey that the elementary taxes are supplemented by a tax on the whole income. This survey deals exclusively with enterprises having an establishment in Roumania. The law makes no provision to cover the case of enterprises which have only their seat of management in Roumania and which operate entirely in other countries. Nor, in fact, are there any enterprises of this kind, Roumania being a comparatively young country which possesses little capital and tends rather to import capital than to export it.

2. TAXATION OF CERTAINS KINDS OF INCOME.

(a) *Dividends.*

Companies having their head office in Roumania are bound to pay the tax on income from personal property on the dividends declared payable, even if they are not actually distributed without

regard to the nationality or domicile of the shareholders. When paying the dividends, they withhold the amount of the tax which they have paid in advance to the Treasury.

Roumanian branches which do not distribute dividends, but transfer their profits to the head office abroad, are not required to pay the tax on personal property, except when the foreign seat distributes a dividend, in which case the branch in Roumania has to pay the tax on the part of the profits earned in Roumania (Article 23, *ad* paragraph 48 of Instructions, *Official Monitor*, No. 793, of April 11th, 1929).

(b) *Interest.*

In virtue of the real character of the tax on personal property, interest on bonds and secured and unsecured loans is taxable when the debtor has his seat in Roumania. The tax is deducted at the source.

In the case of interest being payable to companies, it is not included among the income subject to the elementary tax on commercial and industrial income, but only to the complementary tax of the same schedule.

Foreign capital lent to a Roumanian enterprise or deposited in a Roumanian bank enjoys certain fiscal advantages (see page 389).

(c) *Directors' Percentages.*

If fees paid to directors are of a fixed amount and bear no relation to the profits of the company, they are subject to the tax on salaries and wages. If, on the contrary, these fees vary according to the profits of the company, they are regarded as income from personal property and are taxed as such.

(d) *Royalties for Use of Patents, Copyrights, Trade-marks, Secret Processes and Formulæ and Similar Income.*

All royalties for the use or the exploitation of incorporeal property rights (patents, copyrights, trade-marks, goodwills, mining and oil concessions, etc.) are subject to the tax on personal property, whether payable in cash or in kind. The taxation of such income follows the same rules as set forth in connection with interest under (b).

(e) *Rents from Real Estate, Mining Royalties and Similar Income.*

Rents derived from the lease of real property are assessable to agricultural tax or to the tax on buildings, according to the nature of the property. Exception is made for rents from the buildings of companies for the promotion of cheap building, which are assimilated to income from industrial enterprises and are taxed at a lower rate. Rent from the lease of industrial plant, business premises or mining concessions is assessable to the tax on income from personal property, being regarded as an assignment of rights.

Income from buildings intended and exclusively used for some industry (factories, workshops, etc.) is exempt from the tax on buildings, since it is considered to be part of the industrial or commercial income of the enterprise.

If the owners of real estate are domiciled abroad, the tax on agricultural income or buildings is doubled, irrespective of the taxpayer's nationality.

Income from real property belonging to a share company which has already been assessed to a schedular tax is not subject, like other income of the company, to the elementary tax on commercial and industrial income. Such income continues, however, to be subject to the commercial surtax.

Forests come under a special regime.

(f) *Gain derived from the Purchase and Sale of Real Estate, Securities and Personal Property.*

1. Profits accruing from real estate transactions are subject to the tax on commercial and industrial income, if the company or individual selling or buying habitually deals in real estate. On the contrary, isolated sales are not taxed.

2. Profits derived by a share company from the sale or purchase of securities are considered as part of its general profits and assessable to the tax on commercial and industrial income. Individuals who receive such income incidentally are liable to the tax on income from personal property. If they are permanently engaged in the purchase and sale of securities, the proceeds are assessable to the tax on commercial and industrial property.

3. What has been said in connection with the taxation of income derived from transactions in securities also applies to profits obtained through the purchase or sale of other personal property.

(g) *Salaries, Wages, Commissions and Other Remuneration for Services.*

Persons domiciled abroad who work on behalf of others are taxable in Roumania on account of the remuneration which they receive for such services, if the work has been accomplished in Roumania or if the remuneration has been paid there. When they are domiciled in the country, they are also taxable for all remuneration, whether derived from abroad or from the country.

(h) *Income from a Trust.*

Trusts, as understood by Anglo-Saxon law, are unknown in Roumania, and the law contains no special provisions as regards income derived from such institutions. It is therefore taxed like any other commercial or industrial income of the enterprises which receive an income from a trust.

(i) *Income from the Carrying-on of a Business or Industry through:*

1. *A Commission Agent or Broker.* — In this case, the enterprise is subject to the tax on commercial and industrial income if it owns a depot for the merchandise to be sold in Roumania. In such event, the tax is collected from the commission agent or the broker. If the enterprise has no depot, it is exempt from tax. It should be noted that these agents are separately taxable on account of their own professional earnings.

2. *A Local Dealer or Distributor.* — What has been said in connection with the above applies also here.

3. *A Travelling Salesman, whether or not having Power to conclude a Contract.* — In this case, the foreign company is not taxable, but its agents are taxed in their own names in respect of their professional earnings.

4. *A Local Agent with a Power of Attorney.* — The principles governing tax liability are the same as set forth under 1 above.

5. *An Agent selling out of a Stock belonging to the Foreign Enterprise.* — In this case, the enterprise possesses a depot — *i.e.*, a permanent establishment in Roumania — and is therefore taxable as under 1 above.

6. *A Permanent Establishment of Any Kind.* — Foreign enterprises are always subject to the tax on commercial or industrial income when they possess an establishment of such nature in Roumania.

B. NATIONAL ENTERPRISES.

Those enterprises are national which are incorporated in Roumania in accordance with Roumanian law and have their head office in that country.

Such enterprises are taxable in respect of their entire commercial and industrial income; therefore, both as regards income of this kind derived from abroad and that derived from the country. Income not included among these profits is taxed according to the principles regulating the various schedular taxes described in Part I.

PART III.—METHODS OF ALLOCATING TAXABLE INCOME.

A. FOREIGN ENTERPRISES WITH LOCAL BRANCHES OR SUBSIDIARIES.

I. GENERAL QUESTIONS AND METHODS OF APPORTIONMENT.

As already stated, branches and subsidiaries are taxed in their own names, on the basis of their own profits quite without regard to the general results obtained by the enterprise from its operations as a whole.

(a) BOOK-KEEPING AND ACCOUNTING REQUIREMENTS.

The accountancy is regarded as the first and most important means of establishing the taxable net income of merchants who are required to keep books. If the books are regularly kept, the Assessment Committee is bound to take them into consideration as the basis of taxation. The accounts may only be disregarded in certain cases, of which the following are examples :

(a) Omission to enter invoices under proper dates (Bucharest Court of Appeal, Section IV, Decision No. 39, of March 24th, 1928) ;

(b) Obvious errors or fictitious entries in the books or balance-sheet (Court of Cassation, Section III, Decision No. 2200, of November 19th, 1924) ;

(c) Non-approval by the general meeting of the balance-sheet and profit-and-loss account of share companies (Târgul-Muresh Court of Appeal, Decision No. 1938, of March 23rd, 1926) ;

(d) Discrepancies between entries in the day-book and those in the other books (Bucharest Court of Appeal, Section IV, Decision No. 26, of February 24th, 1925) ;

(e) Incomplete entries in the books and lack of the necessary documentary evidence (Bucharest Court of Appeal, Section IV, Decision No. 84, of June 14th, 1928) ;

(f) Blank pages in the day-book at the end of each month giving rise to presumption of fraud (Court of Cassation, Section III, Decision No. 36, of January 9th, 1925) ;

(g) Omission to make daily entries of transactions (Bucharest Court of Appeal, Section IV, Decision No. 15, of January 20th, 1927) or if goods are not entered at the time of their delivery (Bucharest Court of Appeal, Decision No. 50, of May 31st, 1928) ;

(h) Discrepancy between the taxpayer's return and the balance-sheet or profits as shown by the accounts (Cluj Court of Appeal, Decision No. 2905, of February 1925, and Court of Cassation, Section III, Decision No. 1542, of September 27th, 1924).

In every case where the Assessment Committee disregards the evidence of the accounts, it must be able to give satisfactory reasons for so doing.

(b) METHODS OF ALLOCATION.

1. *Method of Separate Accounting.*

The taxable income of branches or subsidiaries of foreign enterprises is as a general rule determined separately. The assessment is made, in principle, on the basis of the return filed by the taxpayer, which should be supported by various documents (balance-sheet, profit-and-loss account and any documentary evidence the branch can furnish). The Assessment Committee is entitled to check the books, if this is deemed necessary.

As a rule, no enquiry is made into the basis of the prices at which goods have been invoiced by the parent enterprise to its branch or subsidiary, but, if the invoiced prices appear out of proportion, they may be corrected. In no case may any remuneration, commission or royalty paid by the branch to the parent enterprise be deducted from profits of the latter.

2. *Empirical Methods.*

If, for any of the reasons given under (a) above, the account books are disregarded, or if the branch keeps no regular accounts, profits are assessed empirically. The following are the bases of assessment which may be used :

(i) *Comparison of Turnover of Branch to that of Similar Enterprises* (Article 39, *Official Monitor*, No. 288, of December 25th, 1929). — By "turnover" is meant the total sum realised from sales of every kind during the preceding year.

When the Assessment Committee uses this method, it determines the income presumptively by taking as the basis the ratio of profits realised by similar enterprises in relation to their turnover. The fixing of this ratio rests entirely with the Committee (Bucharest Court of Appeal, Decision of August 7th, 1927. *Bulletin of Court of Appeal*, No. 9, of 1927).

(ii) *Comparison with Other Taxpayers.* — If it is impossible to ascertain the turnover, the income may be determined on the basis of the income of other taxpayers of the same class and standing, regard being had to the rent or rental value of the establishment where operations are conducted (Article 39, amended by Law of December 23rd, 1929, and by Law of January 1st, 1932).

3. *Method of Fractional Apportionment.*

Roumanian law contains no provision for the use of this method which is not employed in Roumania.

4. *Requirements for Selection of Methods and Value of the Various Methods.*

The administration is not legally entitled to choose between the three methods described under (i) and (ii). The authorities are bound to take account of the taxpayer's return and of the documents he submits. If accounts are regularly and conscientiously kept, taxation must be based exclusively upon the books.

Only if the accounts are not regular or if no books are kept at all may recourse be had to the empirical method, and the basis employed for assessment may be either that of the turnover or that of comparison with similar enterprises.

Further, recourse to assessment by comparison with other enterprises on exterior signs is only permissible in cases where it is impossible to use the turnover as a basis. Thus the law expressly fixes the preference to be given to the different methods.

The system of schedular taxes has only been in force since 1923. It is therefore impossible, in view of its short existence and of the instability of economic conditions, to pass definite judgment upon the general results of the law or on a large number of details.

It is, however, thought that assessment on the basis of accounts is the fairest method and furnishes the surest guarantee against fiscal evasion. It has drawbacks, however, for the taxable income is determined in a different manner for enterprises which keep accounts and for those that do not, which may result in placing an unequal fiscal burden upon two similar enterprises. It should, moreover, be added that this method is slow, expensive and complicated and implies a certain inquisitorial procedure which may be abused and is in any case felt as a serious nuisance.

(c) APPORTIONMENT BETWEEN BRANCH AND PARENT ENTERPRISE.

It has already been explained that, in Roumania, the situation of the seat of the enterprise entails no fiscal consequences, the tax being levied at the place where the branch is situated and exclusively on the profits earned by it.

1. *Apportionment of Gross Profits of Branch to Real Centre of Management abroad.*

The Roumanian branch being taxed as if it were an independent enterprise, in no case is any fraction of profits apportioned to the centre of management abroad, nor is any account taken of the source from which the branch's profits are derived.

2. *Apportionment of Expenses of Real Centre of Management to Branch.*

Interest Charges.

When an enterprise has a general debt, the interest payable thereon is ascribed solely to the real centre of management abroad. Even when the management lends the branch part of its capital, the latter cannot deduct the interest from its profits assessable to elementary tax on commercial and industrial income, since Article 31, paragraph 2, of the law requires that the creditor shall have a separate legal entity from that of the debtor. But, if the branch borrows money direct from a creditor other than the company to which it belongs, the interest on the debt may be deducted from the branch's profits.

General Overhead.

The principle being that the branch is taxed as if it were an independent enterprise, general overhead expenses of the foreign centre of management are only taken into account within a very limited measure to be determined freely by the Assessment Committee.

3. *Apportionment of Net Profit from Branch to Deficitary Parent and vice versa.*

As a branch established in Roumania is taxed as if it were an independent enterprise, no account is taken, for the purpose of taxation, of whether the whole enterprise has realised profits or is working at a loss. All that counts is the result of the operations of the Roumanian branch. By reason of the same principle, if the branch is working at a loss, it is not taxed in Roumania.

(d) APPORTIONMENT BETWEEN PARENT ENTERPRISE AND SUBSIDIARIES.

A subsidiary organised in accordance with Roumanian law is treated as a Roumanian company and the Treasury does not consider whether it is financed or controlled by a foreign company. Its statement and balance-sheet are checked in the manner described above and may, if necessary, be corrected.

II. APPLICATION OF THE METHODS OF ALLOCATION IN SPECIFIC CASES.

(a) INDUSTRIAL AND COMMERCIAL ENTERPRISES.

Roumanian law does not distinguish between profits according to their origin (manufacture, purchase and sale). Therefore, although the goods may be manufactured or bought abroad, the whole profit at the time of sale in Roumania is liable to tax. Similarly, if goods are manufactured in Roumania and sold abroad, the entire profit from manufacture and sale is taxable in Roumania. If, however, the enterprise makes a reasonable distribution of these various profits in accounts which are recognised to be regular, the tendency in practice is to take account of such distribution.

1. *Selling Establishments.*

As regards local establishments selling in national markets, the basis of assessment is, as already stated, the declared income as checked by the accounts, without regard to any existing links between the local establishment and the parent enterprise, centre of management abroad, etc. Accordingly, the tax is levied on the total income of the local establishment, without regard to the fact that the enterprise buys or manufactures abroad the goods sold in Roumania.

In the case of a sales establishment belonging to a foreign enterprise and selling abroad, it is taxed on the entire amount of the profits as shown by its accounts, and consequently on the total amount of its profits derived from sales made abroad.

2 and 3. *Manufacturing and Processing Establishments.*

If a foreign enterprise owns in Roumania a factory, works or any other establishment manufacturing or processing goods which are sold abroad, the tax is only levied on the profits shown in the accountancy of the Roumanian establishment. Taxation of the Roumanian establishment, therefore, only takes place if profits are shown in its books.

4. *Buying Establishments.*

When a foreign enterprise buys goods in Roumania, through a permanent establishment, with a view to manufacturing and/or selling them abroad, it is only taxable if the accounts reveal a profit.

Purchases made by a foreign enterprise in Roumania which are not followed by a corresponding sale in the country are not taxable, because the commercial transaction is not complete and also because a presumed profit, that is, a profit whose existence is not established, may not be taxed.

5. *Research or Statistical Establishments, Display Rooms, etc.*

If a foreign company has an establishment in Roumania which does not directly engage in any profit-making transactions, but contributes indirectly to the realisation of profits — e. g., a statistical bureau, a display room — the foreign company is not taxable, since it engages in no commercial or industrial activities in Roumania. This applies also to the Roumanian establishment itself.

(b) OTHER KINDS OF ENTERPRISE.

As regards banking and insurance companies and land or water transport enterprises, the general rules set forth above (see pages 400 and 401) are applied — that is, in principle, the basis of allocation is constituted by the special balance-sheet of the establishment situated in Roumania, subject to corrections and amendments.

Railroads belonging to the State, questions of taxation only arise in connection with the International Sleeping-Car Company. This company is taxed on the basis of its receipts in Roumania.

No question relating to foreign gas, light and power companies has come before the tax authorities. Telephones are exploited under a concession and, under the terms of the agreement entered into with the State, the concessionary company is exempt from all tax.

Mining and oil companies are all Roumanian.

B. NATIONAL ENTERPRISES WITH BRANCHES OR SUBSIDIARIES ABROAD.

There are few Roumanian companies which have branches or subsidiaries abroad, for Roumania is too new a country to have been able to make investments abroad.

I. GENERAL METHODS OF ALLOCATION.

The same methods of allocation in force for foreign enterprises are applicable to national enterprises.

The profits of branches or subsidiaries abroad are only taxed in Roumania when they are added to the profits of the Roumanian enterprise and are amalgamated therewith. There is therefore no occasion for special computation or determination as the taxable profits are those which are ascertainable from the accounts of the enterprise, and income from abroad is taxed in the same way and under the same conditions as income derived from Roumania.

II. ALLOCATION OF PROFIT TO REAL CENTRE OF MANAGEMENT WITHIN THE COUNTRY.

The question of the allocation of the special ratio of the profits of the branch situated abroad to the Roumanian enterprise to which it belongs does not arise. The entire amount of the profits of the branch are taxable as soon as they appear in the accounts.

C. TRUSTS AND HOLDING COMPANIES.

The law makes no provision for holding companies, which are therefore regarded as ordinary companies, and, further, both in the case of a Roumanian holding company having subsidiaries abroad and of foreign holding companies having subsidiaries in Roumania, the rules set forth above are applied.

On the other hand, with regard to the taxation of subsidiaries, no account is taken of whether or not they are controlled by a holding or trust company, and taxation is carried out exactly in the same manner as for any other company.

Further, it should be noted that holding companies are, like any other companies, taxed on their profits, after deduction of the income derived from the securities of subsidiaries, if these securities have already been subject to the tax on income from personal property in Roumania.

Annex.

TABLE OF TARIFFS.

	State tax ¹	Addi- tional taxes ²
	Percentage	
I. TAX ON INCOME FROM AGRICULTURAL PROPERTY.		
Income from agricultural property and assimilated thereto, worked by the owner	6	7
Income from the renting of agricultural property :		
Normal rate	7	7
Rate applicable to the income of properties belonging to orphans or of properties rented to peasants' associations or co-operatives.	6	7
Income from forests exploited or leased by their owners	8	7
Income from the felling of forests, except when the forests are legally destined therefor	15	7
Income from rural property belonging to persons living abroad	24	7
II. TAX ON INCOME FROM BUILDINGS.		
Normal rate	10	8
Rate applicable in the case of property belonging to persons living abroad.	20	8

¹ Eventually including the 10 and 20 per cent surcharges prescribed by the Law of January 1st, 1929 (*Official Monitor*, No. 1).

² Levied on behalf of the provinces, communes, chambers of commerce and other public bodies.

III. TAX ON INCOME FROM SECURITIES.	State tax	Addi- tional taxes ¹
	Percentage	
Income from movable capital and assets assimilated thereto	16.50	3
Income from registered shares	13.2	3
Interest on bank deposits at three months or less	11	Nil
Deposits at more than three months.	5.5	Nil
Income from deposits belonging to foreigners with Roumanian banks .	5	Nil
Income from mortgage bonds or bonds issued by the " Cheap Housing Society " :		
When the rate of interest amounts to 5 per cent	8.8	Nil
When the rate of interest amounts to 10 per cent.	5.5	Nil
Annuities on eviction indemnities.	5.5	Nil
IV. TAX ON INDUSTRIAL AND COMMERCIAL INCOME.		
I. <i>Elementary tax.</i> ²		
Industrial and commercial profits.	10	6
Profits exclusively industrial	8	6
Profits of banks and credit institutions	12	6

¹ Levied on behalf of the provinces, communes, chambers of commerce and other public bodies.

² New enterprises are exempt from tax during their first five years if their yield does not exceed 8 per cent of their capital, and they are entitled to a reduction by half of the tax if their yield, although it is over 8 per cent, does not exceed 10 per cent.

2. Complementary Tax.

Rate of the yield of the taxed enterprise (percentage in relation to the assets employed in the business)		Rate of tax applicable to the total taxable profits	
Between	And	In the case of share companies ¹	In the case of individuals ²
10	12	0.50	—
12	13	0.75	—
13	14	1	—
14	15	1.50	—
15	16	2.	0.50
16	18	2.50	1
18	20	3	1.50
20	22	4	2
22	25	5	2.50
25	30	6	3
30	35	7	3.50
35	40	8	4
40	45	9	4.50
45	50	10	5
50	60	11	6
60	70	12	7
70	80	13	8
80	90	14	9
90	100	15	10
100	120	16	11
120	160	17	12
160	200	18	13
200	250	19	14
250	300	20	15
300	350	21	16
350	400	22	17
400	450	23	18
450	500	24	19
Over 500		25	20

¹ Complementary tax is reduced by 25 per cent in the case of share companies which grant to their staff, either in virtue of their statutes or of the law, a share in the net profits of at least 25 per cent.

² Complementary tax applies to enterprises not belonging to share companies only if the profits exceed 15 per cent of the assets employed in the business.

V. TAX ON SALARIES AND WAGES.

Amount of the taxable remuneration	State tax	Additional taxes ¹
	Percentage	
Salaries not exceeding 4,000 lei per month.	4	Nil
Salaries exceeding 4,000 lei per month	8	Nil

VI. TAX ON INCOME FROM PROFESSIONS
AND OCCUPATIONS NOT SUBJECT TO OTHER TAXES.

Income from liberal professions.	8	4
Income from other professions	6	4
Income from literary, artistic, scientific, etc., works.	5	4

VII. GRADUATED TAX ON TOTAL INCOME. ²

Taxable income		Tax corresponding to the first figure of the "income" column		Tax applicable to the portion of income included between the two figures of the "income" column	
Between	And	Percentage	(In lei)	(In lei)	For each whole amount of (In lei)
(ooo's omitted)	(ooo's omitted)				
10	20	1	200	15	1,000
20	30	1.166	350	15	1,000
30	40	1.25	500	15	1,000
40	60	1.60	960	23	1,000
60	80	2	1,600	64	2,000
80	100	2.50	2,500	90	2,000
100	150	3.25	4,875	237.50	5,000
150	200	4	8,000	312.50	5,000
200	300	6.25	13,600	530	5,000
300	400	7.60	30,400	590	5,000
400	500	9	45,000	740	5,000
500	600	10.50	63,000	900	5,000
600	700	12	84,000	1,050	5,000
700	800	13	104,000	2,000	10,000
800	1,000	14.40	144,000	2,000	10,000
1,000	1,500	16.80	252,000	4,320	20,000
1,500	2,000	18.00	360,000	4,320	20,000
2,000	3,000	19.20	576,000	10,600	50,000
3,000	4,000	20.40	816,000	12,000	50,000
4,000	6,000	21.60	1,296,000	12,000	50,000
6,000	8,000	22.80	1,824,000	13,200	50,000
8,000	10,000	24	2,440,000	14,400	50,000

Over 10,000,000, 36 per cent of the amount in excess of 10,000,000 lei.

¹ Levied on behalf of the provinces, communes, chambers of commerce and other public bodies.

² The non-taxable and deductible minimum is 9,000 lei. The tax is increased by 5 per cent in the case of bachelors and childless widowers between 30 and 55 years of age.

SWITZERLAND

BY

J. RUOF,

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INTRODUCTION.

1. The Swiss Confederation is a federative State consisting of twenty-two cantons, three of which are divided into half-cantons. The latter being sovereign to the same extent as the undivided cantons, there are thus twenty-five States, but their sovereignty is subject to restrictions in favour of the Federal State.

2. In Switzerland, fiscal sovereignty rests with the Confederation and with the twenty-five cantons and half-cantons. Each of the latter has its own fiscal laws, but its fiscal sovereignty is subject to certain restrictions expressly provided for by federal law. The most important restrictive clause in the Federal Constitution is that contained in paragraph 2 of Article 46, which establishes the principle of the inadmissibility of double taxation as between cantons. This article in the Constitution does not apply internationally nor as between communes (duplication of taxes by several communes in the same canton). From the international point of view, however, the Federal Tribunal has decided that real property situated abroad is not subject to cantonal or communal taxes on property or income, unless the State where the property is situated levies a similar tax ¹.

3. As regards taxes on individuals (property-tax and income-tax), the Confederation has only exercised its fiscal sovereignty in exceptional cases. In order to meet the fiscal consequences of the world war, it was decided to levy the first war-tax (1915 and 1917), the tax on war profits (1915-1920) and the new extraordinary war-tax (1921-1932). Of these three taxes, only the last is now in force, and that expires at the end of 1932. Thenceforth, the taxation of property and income will be reserved, as before the war, exclusively to the cantons, the stamp duty on coupons, which is imposed on the yield of certain forms of capital, not being in the nature of income-tax. It does not therefore seem necessary in the present report to explain the new extraordinary war-tax. Its structure, moreover, does not differ in essentials from the systems in force in most of the cantons.

4. In the cantons, taxes are levied not only by the State, but by the public corporations. These public corporations are the communes and, in some cantons, the districts (Schwyz, Inner Appenzell). While French Switzerland knows only one kind of commune — the political (except in the canton of Fribourg, where the parish plays a part) — the rest of Switzerland has a large variety of communes created for special purposes, such as public education, welfare, worship, etc. These communes have the right to impose taxes, and are, as a rule, obliged to do so in order to perform their allotted functions. In some cantons, the taxpayer, in addition to State taxes, pays property- and income-tax to six different public bodies.

¹ *Collected Judgments of the Federal Tribunal*, 1918, Volume I, page 18; 1920, Volume I, page 417.

The constitutions of the cantons grant these communes a measure of autonomy, which is determined, as a rule, by cantonal legislation. This same legislation generally fixes the principles of communal taxation. As regards property- and income-taxes, these principles are as nearly as possible the same as those underlying cantonal taxation ; the assessment of the cantonal tax is normally the basis of the communal tax. In some cantons, communal taxes are imposed as additions (*centimes additionnels*) to cantonal taxes ; in others, the commune fixes the rate to be applied to the assessment as laid down by the canton for individuals and companies liable to taxation in the commune. The additional tax (*centimes additionnels*) and the tax rate fulfil the same purpose, and the amount of both is determined by the competent authorities of the communes according to the latter's fiscal needs.

5. The function of the income-tax in countries where it is not supplemented by a property-tax is discharged in Switzerland by these two concurrent taxes. In many cantons, the property-tax is more important than the income-tax. It is the principal tax ; while the tax on income, which is only imposed on the product of labour, is in the nature of a supplementary tax. In other cantons, the income-tax is the main tax, and the property-tax serves as an additional charge intended to weigh more heavily upon unearned than upon earned income.

The co-existence of these two taxes will necessitate a description, not only of the income-tax, but of the property-tax.

PART I. — GENERAL DESCRIPTION OF THE PROPERTY-TAX AND INCOME-TAX SYSTEM.¹

I. RELATIVE IMPORTANCE OF INCOME-TAX AND PROPERTY-TAX IN THE SWISS FISCAL SYSTEM AND COMPARISON OF THEIR YIELD.

(a) The following are the chief resources of the public corporations :

Confederation. — Taxes ; yield of assets (landed property and capital) ; yield of public enterprises (posts, telegraphs, telephones, mint, etc.) ; fees ; product of sales ; reimbursements, etc.

Cantons. — Taxes ; yield of assets ; revenue from landed property, capital, State banks and industrial enterprises ; yield from monopolies (salt, shooting, hunting, fisheries, mines) ; fees ; product of sales ; grants by the Confederation and share of Federal taxes ; repayments and contributions by third parties, etc.

Communes. — Taxes ; yield of assets ; revenue from landed property, capital and industrial enterprises (gas, electricity and waterworks, tramways) ; fees ; product of sales ; grants by the Confederation and the canton and share of cantonal taxes ; repayments and contributions by third parties, etc.

(b) The tax contribution towards the budgets is shown by the following figures :

Confederation. — In 1928, out of receipts totalling 412 million Swiss francs, 343 million, or 83.2 per cent, were furnished by taxes.²

Cantons. — Out of gross revenue of 580.7 million francs in 1926, taxation produced 262 million, or 45.1 per cent.

Communes. — There are no available figures to show the contribution of taxes towards the communal budgets, but it may be taken as not less than the cantonal figure.

(c) The following are the principal taxes at present in force :

Confederation. — Customs duties, stamp duties, new extraordinary war-tax.

Cantons. — Taxes on income and property, taxes on gifts and inheritances, duties on the transfer of immovable property and the registration of mortgages, cantonal stamp duties, licence fees for public-houses and the sale of alcoholic beverages, licences for hawking and trading, taxes on water-power, tax on motor-cars, bicycles and carriages, dog-tax.

¹ Legislation in force on June 1st, 1933.

² See *Statistiques de la Suisse*, Volume 5, published by the Federal Statistical Bureau, containing statistics of Confederation finances in 1913 and from 1920 to 1928 (page 16, columns 2 and 4). In column 2, under Department of Posts and Railways, the figure 231,940,000 francs, representing gross receipts, should be replaced by 10,074,000 francs, representing net yield.

Communes. — Taxes on income and property ; gift and inheritance duties (in some cantons only), transfer duties, taxes on unearned increment on real estate value, entertainment-tax, dog-tax.

The taxes on property and income provide the cantons with more than 75 per cent, and the communes with more than 95 per cent, of the total receipts from taxation, as will be seen from the following table.

(d) Revenue from taxation in 1928¹ :

(In millions of Swiss francs.)

	Confederation	Cantons	Communes	Total
Yield from all taxes.	359.6	275.8	247.6	883.0
Taxes on property and income :				
Actual figures.	19.9	208.4	234.0	462.3
Percentage of total yield	5.53	75.56	94.51	52.35

(e) In 1928, the burden of taxation in Switzerland per head of the population was 227.58 francs. Of this amount, 119.14 francs was obtained from taxes on income and property.

2. STRUCTURE OF THE TAX.

(a) HISTORICAL SURVEY.

Property-tax was levied in Switzerland, as a special measure, in the Middle Ages. It practically disappeared in the course of the seventeenth and eighteenth centuries, but was revived after the establishment of the Swiss Republic in 1798. Together with other direct taxes, it was intended to replace revenue which had hitherto been obtained from the vanishing feudal dues. The system finally adopted by the Swiss Republic included the land tax, the tax on buildings, licence-fees for trade and industry, a stamp duty on bonds and the tax on salaries. Under the Act of Mediation, which succeeded the Swiss Republic in 1803 and which restored the cantons abolished by the latter, direct taxes were, as far as possible, abandoned in favour of the old feudal dues, and this policy was maintained during the Restoration period between 1815 and 1830, which preceded the Regeneration period. At this time, the property-tax, for historical and economic reasons, figured very prominently. In the first place, it had already proved its worth. Again, Switzerland was at that time a mainly agricultural country, and the incidence of a tax on fortunes fell upon almost the whole population. Income-tax, however, was not long in following though its function was, as in many cantons it still is, supplementary. As G. Schanz said in his book *Die Steuern der Schweiz* (Volume I, page 53), it was an article of faith in Switzerland to take property as the basis for the assessment of direct taxation. By "property" was to be understood, generally, the whole of a taxpayer's real and personal property, including intangible assets, after deducting liabilities (see Georg SCHANZ, Volume I, pages 1 *et seq.* of *Die Steuern der Schweiz*. 1890: J. G. Cotta'sche Buchhandlung, Nachfolger, Stuttgart).

As already mentioned in the introduction, Switzerland has twenty-five cantons, each with its separate laws. In many of these cantons, the communal system of taxation differs in some respects from the cantonal system. It would take too long to outline the fiscal structure of each canton

¹ *Statistiques de la Suisse*, published by the Federal Statistical Bureau, Volume 9, a study published by the Federal Administration of Taxes on the fiscal revenue of the Confederation, cantons and communes in 1926 and 1927 ; price 1 franc 50 centimes.

and then to add the special features of communal taxation. Nor would such a description be of any great interest in the case of the many cantons which have no close economic relations with foreign countries. For our purpose, it is enough to group the cantons in classes and to give the essential particulars for each class, adding details in the case of certain cantons important by reason of their economic relations with foreign countries.

Generally speaking, the taxes levied by cantons and communes on property and income are personal taxes — *i.e.*, taxes adapted to the economic position of the taxpayer.

(b) CANTONAL TAXES.

(*aa*) Starting with the subject-matter of taxation, the fiscal systems in force in the cantons may be classified in six groups

First Group. — General tax on income (total income) and complementary general tax on property (total net property). Both are graduated. This system obtains in the following cantons : Zurich, Lucerne, Uri, Solothurn, Basle-Urban, Basle-Rural and Geneva.

Second Group. — General tax on property (total net property) and tax on that part of income consisting of the product of labour, of income on property in excess of 4 per cent or 5 per cent of the fortune, and of annuities and pensions. Both taxes are graduated. Cantons : Upper Unterwald, Schaffhausen, St. Gall and Thurgau.

Third Group. — General tax on property (total net property) and tax on product of labour, annuities and pensions. Both are graduated. Cantons: Lower Unterwald, Glarus, Zug, Outer Appenzell, Inner Appenzell, Grisons, Aargau, Ticino, Vaud and Neuchâtel.

(*Note.* — In the canton of Grisons, the product of agricultural labour is exempt. In the canton of Zug, the tax on the product of labour is replaced by a cantonal licence-fee payable by persons operating a commercial enterprise, this fee being fixed according to the fiscal capacity of the taxpayer.)

Fourth Group. — Special tax on property (real property and securities, such as shares, bonds, loans and deposits) and tax on product of labour, annuities and pensions. Both taxes are graduated. Cantons : Fribourg and Valais.

Fifth Group. — Special tax on property (real property, interest-bearing loans secured on immovable property situated in the canton), special tax on product of labour (excluding agricultural labour) (first-class income) and special tax on income from capital (except capital secured on real property situated in the canton), gains from speculation and capital profits (second-class income). The taxes are graduated. Canton : Berne.

Sixth Group. — General tax on property (total net property) and special tax on annuities and pensions, neither tax being graduated. Canton : Schwyz.

(*bb*) The cantons of Zurich, Lucerne, Fribourg, Basle (Urban and Rural), Schaffhausen, St. Gall, Ticino, Vaud, Valais and Geneva have established a special fiscal system for companies and co-operative societies. The working capital and reserves (revealed and hidden) are liable to a tax on capital, and net profits to a tax on profits. The former tax replaces the property-tax payable by other classes of taxpayer and the profits-tax takes the place of income-tax. The cantons of Fribourg, Basle-Urban, Basle-Rural, Valais and Geneva further tax capital that is not paid up.

The tax on capital is proportional, except in the cantons of Basle-Rural and St. Gall. The tax on profits is graduated, the rates being fixed in the ratio of net profits to working capital, with a maximum limit.

The great majority of cantons grant fiscal facilities to holding companies (*sociétés de participation*). Seven cantons levy part only of the tax payable according to the law ; twelve tax capital at reduced rates and eleven exempt profits. Details are given in the Table of Tariffs annexed to the present study.

The term *société de participation* (holding company) includes any share company (*société anonyme*), limited partnerships by shares (*société en commandite par actions*), or co-operative association (*société coopérative*), whose assets are exclusively or mainly invested in holdings in other companies of the same legal nature. These holdings (*participations*) may consist in shares or bonds.

Some cantons grant fiscal facilities to *sociétés de domicile* (companies of domicile). A *société de domicile* is a share company or a co-operative association which has only its domicile in a canton and does not carry on there any industrial or commercial activity. In those cantons, holding companies enjoy fiscal privileges granted to companies of domicile.

(cc) The cantons, whether they have a special system for taxing share companies and co-operative societies or not, not only tax the capital and profits of these companies and societies, but at the same time tax the shareholders and members on the value of their shares or beneficiary interests and, according to the system (Class I above), also tax the yield of these securities. In fiscal law, the possession of shares in a share company or a beneficiary interest in a co-operative society is considered as an investment of capital and not as participation in a company. The owner of such shares or interests is liable to tax on them just as he is liable on bonds or deposits. In law, this duplication of tax does not constitute double taxation, and the Federal Tribunal has always held that Article 46, paragraph 2, of the Federal Constitution prohibiting double taxation as between cantons is not applicable to this duplication. A few cantons, however, avoid recourse to it and exempt their taxpayers from payment of cantonal taxes on shares in companies and associations subject to taxation in the canton. These cantons are Schwyz, Upper and Lower Unterwald, Solothurn, Inner Appenzell, Grisons, Thurgau, Ticino and Neuchâtel. The exemption applies to the tax on property. Solothurn, the only one of these cantons that taxes income from securities of this class, extends the exemption to such income.

(dd) Duplication of taxes occurs in another form in the cantons of the first group and to some extent in those of the second. A taxpayer possessing a certain property is taxed on the net value of that property as well as, in the form of income-tax, on the income from it. As mentioned under paragraph 5 of the Introduction, the tax on property is intended in these cantons to illustrate the principle that unearned income can support a heavier fiscal burden than earned income.

A similar duplication, though not due to the same cause, affects share companies and co-operative societies in the cantons that impose special taxes on these classes of taxpayer. The capital of the company or co-operative is taxed, as well as the profits.

There is no such duplication in the cantons of groups III and IV. The yield from property is taxed under the property-tax alone and is not assessable to income-tax. The Swiss principle to which reference has already been made is observed in these cantons by a suitable rate of taxation, involving a heavier charge on the yield of the property than it would bear if it were liable to income-tax at the rate corresponding to that yield.

When a taxpayer's income is the result of co-operation between labour and capital, as is the case with agricultural, commercial and industrial enterprises, the cantons in groups II to V avoid a duplication of taxation by allowing the taxpayer to deduct from his income the presumed yield of the capital which he himself has put into his business. This yield is calculated at rates fixed by law and vary from 4 to 6 per cent. This deduction is granted : (1) to all taxpayers, including companies and co-operatives, by the cantons of Berne, Upper and Lower Unterwald, Glarus, Schaffhausen, Inner and Outer Appenzell, St. Gall, Grisons, Aargau, Thurgau, Ticino and Neuchâtel ; (2) to all taxpayers, except companies and co-operatives, by the cantons of Vaud and Valais.

(ee) Except Schwyz, all the cantons impose graduated taxes. The graduations are separate for the two kinds of tax (tax on property and income-tax) and are adapted to the object of taxation. Only the cantons of Berne, Upper Unterwald, Solothurn and Aargau have a single graduation, the scale of which is based on the combined total of the tax on property and the income-tax.

(c) COMMUNAL TAXES.

In most of the cantons, the structure of the communal taxes on property and on income coincides with that of the cantonal taxes. In the cantons of Solothurn and Grisons, however, communes have the right to regulate their taxes on property and income differently from the cantonal taxes. In the canton of Glarus, communes may tax property but not income, and in Valais the communes levy an industrial duty (*taxe industrielle*) in the place of a tax on income (product of labour).

In the following cantons the communal taxes on property and on income are graduated differently from the corresponding cantonal taxes. Graduation is forbidden to the communes in the cantons of Uri, Basle-Rural, Valais, Zug (only for tax on property), St. Gall (only for tax on property) and Schaffhausen (parishes and larger communes). The communes in the cantons of Fribourg, Vaud and Neuchâtel are allowed to impose either proportional taxes or graduated taxes. In the cantons of St. Gall (for income-tax only), Ticino and Schaffhausen, the communal scale of graduation differs from the cantonal scale.

The communes in the cantons of Zurich, Fribourg, Inner Appenzell, Grisons and Vaud are authorised to levy a special tax on real property; communes in the cantons of Vaud and Geneva may impose an industrial duty on enterprises operated within their territory.

In the following cantons the communes are required to accord to companies and co-operatives different treatment from that granted by the canton. In the canton of Glarus communes are not allowed to tax profits. In the cantons of Glarus, Zug (for property) and Ticino the taxes are not graduated but only proportional. Many communes in the cantons of Grisons, Solothurn and Vaud have rules which differ widely from the cantonal regulations.

(d) DEFINITIONS.

The terms "property", "capital", "income", "product of labour", "profits" and other expressions used in cantonal or communal legislation as a general description of taxable objects are not defined in the fiscal laws.

By "property" are meant all the objects and rights at the disposal of a person within the meaning of private law¹, unless the law, when enumerating the objects of taxation, defines it otherwise. When (b) (aa) above speaks of a general tax on property (for groups I, II, III, and VI), this does not mean that the whole property is in every case actually the object of the tax. The law often limits the taxable objects and provides exceptions, having regard either to the taxpayer's economic position or to the purpose of articles (household furniture); finally, deduction of debts is allowed, except in particular cases.

As regards "income", many cantons employ this term to indicate the nature of the tax, even if only a part of the income — e.g., the product of labour — is assessable to tax. In order to ascertain the real nature of the tax, the law must in every case be consulted. In the cantons of groups I and II specified above (No. 2 (b) (aa)), the term "income" includes earned and unearned income, from which, to get the real income, must be deducted the necessary expenses.

¹ BLUMENSTEIN, *Schweizerisches Steuerrecht*, Volume I, page 172.

The product of labour is the earned income, and it includes income derived from labour alone and income due to the combination of labour and capital (enterprises) ; the expenditure necessary to obtain the product of labour is deducted.

In relation to companies (*sociétés anonymes*) and co-operatives, the expression "capital" means the capital invested in the company ; this includes statutory capital paid up and revealed and hidden reserves.

The "profits" of these companies must be understood to mean their net profits plus appropriations of the company which the law regards as profits — *e.g.*, excessive depreciations, bonuses to shareholders as a charge on operations, taxes (in several cantons), etc.

See, for example, among cantonal laws :

Property. — Paragraph 16¹, Zurich ; Article 4², Berne ; Paragraph 20³, Basle-Urban ; Article 35⁴, Geneva.

Income. — Paragraph 8⁵, Zurich ; Article 19², Berne ; Paragraph 17³, Basle-Urban ; Article 16⁴, Geneva.

Capital. — Paragraph 31¹, Zurich ; Paragraph 3⁶, Geneva ; Article 68⁴, Geneva.

Profits. — Paragraph 30¹, Zurich ; Paragraph 4⁶, Basle-Urban ; Article 66⁴, Geneva.

3. TAXPAYERS.

(a) INDIVIDUALS.

The obligation to pay cantonal or communal tax (assessability to tax) does not depend upon nationality. An individual is liable if he has his domicile in the canton or, in the absence of domicile, possesses or has the enjoyment of real property, or carries on a business, there. Some cantons claim taxes from persons who make a lengthy stay in their territory⁷. Two or three cantons subject to taxation persons who work in the canton without being domiciled or resident there ; others levy upon persons who, though absent from the country, possess an estate there which is administered by the competent cantonal authorities. These cases do not concern industrial and commercial enterprises belonging to individuals and there is therefore no need to discuss them further.

Individuals are required to pay taxes to the parish, but only to a parish representing their own creed.

In civil law, a person is domiciled at the place where he is living with the intention of settling there. This conception of domicile underlies the jurisprudence of the Federal Tribunal in all cases of inter-cantonal double taxation. Internationally and as between communes, this jurisprudence is not applied ; fiscal domicile is in the place indicated by cantonal or communal legislation. If the

¹ *Gesetz betr. die direkten Steuern* vom 25. November 1917.

² *Gesetz über die direkten Staats- und Gemeindesteuern* vom 7. Juli 1918.

³ *Gesetz betr. die direkten Steuern* vom 6. April 1922.

⁴ Law on Public Contributions, dated March 24th, 1923, as amended by the Law of December 24th, 1924.

⁵ *Gesetz* vom 15. Oktober 1928, *über die Abänderung der Steuergesetze* vom 25. November 1917 und vom 19. Februar 1922.

⁶ *Gesetz betr. die Besteuerung der anonymen Erwerbsgesellschaften*, dated June 23rd, 1921.

⁷ Basle-Rural, paragraph 8, No. 1 (a) and (b), *Gesetz über die Staatssteuer u. die Handänderungsgebühr*, dated August 20th, 1928 ; Berne, Article 17, No. 2, *Gesetz über die direkten Staats- und Gemeindesteuern*, dated July 7th, 1918 ; Fribourg, Article 2 (a), Law of May 7th, 1926, on cantonal taxes ; Valais, Article 12 of the decree of January 15th, 1921 ; Vaud, Article 2 (a), Law on the taxation of property and the product of labour, dated January 24th, 1923 ; Geneva, Article 2 (2) of the Law of March 24th, 1923, on public contributions.

law uses the term "domicile" without defining it, the conception must be accepted as that of civil law. This is the case, for example, in the cantons of Basle¹, Berne² and Geneva³. Many cantons, including Zurich⁴, impose the tax on individuals inhabiting the canton. Persons are deemed to inhabit the canton of Zurich when their stay in one place is more than purely temporary and they have the intention of remaining for a certain time⁵.

(b) PARTNERSHIPS.

There are in Switzerland the following kinds of partnership :

- Joint ventures (*la société simple*) ;
- Partnerships (*la société en nom collectif*) ;
- Limited partnerships (*la société en commandite*).

Joint ventures are not taxed by the cantons, but their members are⁶.

Partnerships (with unlimited liability) and *limited partnerships* have no legal entity, but all the same may, as firms, become creditors or debtors, sue and be sued in the courts and acquire rights of ownership and other real rights, including rights over real estate (Articles 559 and 597 of the Federal Code of Obligations).

Some cantons tax these partnerships, others do not. The former forbear to tax the partners on their respective shares in the partnership (property and income) ; the latter tax them without regard to their domicile. These partnerships are taxed in the following cantons : Berne, Lucerne, Uri, Upper and Lower Unterwald, Zug (*patente* taxes), Fribourg, Solothurn, Grisons, Thurgau, Ticino, Vaud and Neuchâtel. The other cantons do not tax these partnerships but the partners themselves at the place where the partnership has its head office, no matter whether the domicile of the partners is there or not. The tax is levied on the share of property (capital) or on the income derived from the partnership belonging to the partner.

(c) COMPANIES.

Companies are divided into :

- Share companies (*sociétés par actions*).
- Limited partnerships with share capital (*sociétés en commandite par actions*).
- Co-operative societies.

¹ Paragraph 14, No. 1, paragraph 20, No. 1, *Gesetz betr. die direkten Steuern*, dated April 6th, 1922.

² Article 17, No 1, *Gesetz betr. die dir. Staats- u. Gemeindesteuern*, dated July 7th, 1918.

³ Article 2, No. 1, Law on public contributions, dated March 24th, 1923.

⁴ Paragraph 2, No. 1, *Gesetz betr. die dir. Steuern*, dated November 25th, 1917.

⁵ *Kommentar z. Zürch. Steuergesetz*, by E. RICHARD, page 15, published by Polygraph. Institut, Zurich.

⁶ Article 530 of the *Federal Code of Obligations*. — "Association resulting from a contract by which two or more persons agree to pool their efforts and their resources for a common purpose.

"Such association is a joint venture, in the sense in which it is here used, when it has not the distinctive characteristics of one of the other associations governed by the law." These other associations are : partnerships, limited partnerships, share companies, limited partnerships with share capital, co-operative societies.

The joint venture does not possess a legal entity apart from its members. It cannot be a creditor or debtor, nor sue or be sued, nor acquire real or personal property. In the case of a joint venture, it is the members who acquire rights and incur obligations individually. In respect of third parties, an association, properly so-called, does not therefore exist, but simply members held personally responsible for acts performed by them or by their representatives.

They are legal entities and are liable to cantonal and communal taxation, which in fiscal law does not prevent the members of the company from being also taxed on the value of their shares and on the accruing dividend or on the value of their share and on the profit which is distributed to them. Exceptions to this duplication of taxes are given above under No. 2 (b) (cc).

A company formed under Swiss law is taxed in the place where it has its head office. As between cantons, however, the jurisprudence of the Federal Tribunal has conceded, in application of Article 46 of the Federal Constitution (prohibition of double taxation), that companies whose effective and exclusive centre of management is not at the place of the head office are taxable at the place of that centre of management¹.

This jurisprudence does not apply to international double taxation. In these cases, the fiscal domicile of a Swiss company is at the place of the head office, even if the company has its effective centre of management abroad.

A company formed abroad is taxed in Switzerland if it has immovable property or an establishment there. As regards the extent of assessability to tax, the reader is referred to No. 4 below.

It should be added that, in some of the cantons in which companies are subject to a special fiscal regime, the rules governing certain kinds of co-operative associations differ from that regime. This applies to the kind of co-operative associations which realise the principle of economic mutuality, such as consumers' associations and agricultural co-operatives, as opposed to co-operatives which are chiefly or mainly based on capital.

4. TAXABLE PROPERTY AND INCOME.

(a) Cantonal and communal taxes are personal, attaching to the subject and not to the object. The economic allegiance of capital and income is therefore not a factor. Whether capital is invested in Switzerland or abroad and whether the source of income is Swiss or foreign are of no importance from the point of view of their taxation. In two cases, however, economic allegiance does play a part; these relate to real estate and enterprises.

(b) All real property situated in the territory of a canton is subject therein to cantonal and communal taxation. On the other hand, real property abroad belonging to a Swiss taxpayer is exempt from these taxes, provided they are imposed by the State where the property is situated. This rule does not apply to debts secured by mortgage, which under Swiss law are part of personal fortune and are subject to the same fiscal treatment as the latter.

The capital in a commercial or industrial undertaking established in Switzerland and the income derived from it are subject to cantonal and communal taxation, wherever may be the domicile or head office of the *enterprise*. On the other hand, if a taxpayer having his domicile or *head office* in Switzerland is interested as owner or partner in an establishment abroad, the capital invested in it and the income derived therefrom is not, in principle, exempt from cantonal and communal taxes.

(c) The fiscal laws of the cantons do nothing to relieve double taxation due to the fact that a foreign State imposes taxes upon real property and enterprises situated in Switzerland. They are, however, content with taxing the capital put into the Swiss property or business and the income derived therefrom. This system is in force in the cantons of Appenzell (Inner and Outer), Basle-Urban, Berne, Geneva, Grisons, Neuchâtel, Lower Unterwald, St. Gall, Schaffhausen, Thurgau, Uri, Vaud and Zurich.

(d) Real property situated abroad is not taxed twice, because, as already mentioned, Switzerland waives imposition.

¹ *Official Collection of Judgments of the Federal Tribunal, 1919, Volume I, page 190.*

(e) International double taxation due to the simultaneous collection of Swiss and foreign taxes on establishments maintained abroad by taxpayers having their domicile or head office in Switzerland is avoided or alleviated by many of the cantons. Basle-Urban and Schaffhausen grant unconditional exemption to legal entities. Basle-Urban demands reciprocity in the case of individuals and Basle-Rural both for individuals and for legal entities. Grisons, Lower Unterwald (exemption of fortune only) and Thurgau require proof of imposition outside the canton. Geneva and Zurich grant exemption, but only if the cantonal tax represents a certain proportion of the whole tax (in Geneva half, in Zurich one-third). This concession is made both to individuals and to legal entities in respect of the taxable wealth of each of them. St. Gall halves the income-tax due from companies and partnerships. Berne allows the Government to grant relief. Some cantons, such as Glarus, Zug, Basle-Rural, Schaffhausen, Grisons, Ticino and Valais accord to companies which have only their domicile on cantonal territory advantages similar to those granted to partnerships. In relations with Austria this form of double taxation is avoided by the Treaty of October 24th, 1927, concluded between the Austrian Republic and the canton of St. Gall with a view to avoiding certain cases of double taxation. The system embraces cantons which have acceded to the treaty or which have granted reciprocity of fiscal treatment to commercial and industrial undertakings. These include — apart from St. Gall — Zurich, Upper Unterwald, Basle-Urban, Basle-Rural, Inner Appenzell, Aargau, Thurgau, Neuchâtel, Fribourg, and Grisons.

(f) Income from Swiss sources other than real estate or enterprises, and capital invested in these other sources are not taxed provided that the owner is domiciled or has his statutory seat abroad. If, on the other hand, the taxpayer concerned has his domicile or head office in Switzerland, the cantons and communes continue to tax his income derived from a foreign source and the capital invested there, even if the foreign country in question itself taxes these objects.

These principles are invariably applied, even to capital guaranteed by mortgage, to public funds, emoluments paid by the State to its officials and pensions.

A few cantons afford examples of certain unimportant exceptions, but these merely prove the rule. Thus, Article 28 of the Law on public contributions in the canton of Geneva, in the amended text of December 24th, 1924, lays down that persons domiciled abroad shall be taxed on the profits or wages of their work in the canton and on pensions they receive from a public corporation in the canton or a State institution. The canton of Vaud, in Article 2 (c) of the Law relating to the tax on property and on the product of labour, dated January 24th, 1923, taxes income derived by a person domiciled abroad from employment in the canton.

5. ASSESSMENT OF TAX.

(a) DECLARATION BY THE TAXPAYER.

Taxpayers are, in general, required to co-operate in the taxation of their property and incomes by filling up and signing a return, within a prescribed time-limit.

The return must be made annually or at intervals (periods of revision) laid down by law. Some cantons have a standard form of return for all taxpayers; others have forms varying according to the different classes of taxpayers (farmers, *entrepreneurs*, wage-earners, companies).

As a rule, the form of return is the same for property as for income or the product of labour.

Various cantons, *ex officio*, tax immovable property, which is divided into classes. The owner may appeal against the classification and taxation of such property. Taxation is periodic and the value of real property, once fixed, is entered in a special register and cannot be changed until the next revision, except in special circumstances, such as a change in cultivation or the erection of new buildings. In these cantons, the taxpayer must enter in his return the value of his property as thus determined.

Companies and co-operative societies are, as a rule, required to accompany their returns by reports, balance-sheets and profit and loss accounts, if these are published, or, if they are not, to produce extracts from their books, more especially from the balance-sheets and profit and loss accounts. Some cantons require similar documentary evidence from all taxpayers on the Commercial Register (*Registre de Commerce*).

(b) COMPUTATION OF TAXABLE PROPERTY AND INCOME AND ABATEMENTS.

I. *Property.*

(a) Property is taxed according to its content and value at a time specified by the law — generally the beginning of the fiscal period (calendar year) : sometimes, the time when the tax becomes payable.

The preceding information concerning the structure of the tax (No. 2 (b) (aa)) shows that, with the exception of Berne, Fribourg and Valais, all the cantons tax the total net property obtained after deducting from gross property the taxpayer's debts.

The most commonly applied rules of taxation are the following :

Real property is taxed at its marketable value or at the value of its yield ; buildings are, in several cantons, taxed at the value for which they are insured against fire ;

Household furniture and agricultural and professional implements are often exempt from the tax or are assessable on the part of the real value exceeding a certain amount ;

Cattle is taxed at a fair average value or at the mean between market value and yield value ;

Commodities are taxed at cost price or at market value, if this is lower than cost price ;

Machines, tools and the furniture of a business are taxed at purchase price, less depreciation through use ;

Quoted securities, at the quoted rate ;

Securities not quoted on the Stock Exchange, at their nominal value, or at their marketable value, if the latter differs from the former. To determine the marketable value, account is taken of the resulting income, or, where there is no income, of the situation of the enterprise which has issued these securities ;

Claims, including mortgages, bank deposits, balances of current accounts, etc., generally at their nominal value. In assessing the value of bad or doubtful debts, the chances of recovery are taken into account ;

Royalties, at their marketable value, and also at their nominal value, if any ;

Swiss money at its legal value ; foreign money at the rate of exchange quoted ;

Annuities, at their capitalised value ;

Life insurances, at their surrender value ;

As already stated, the taxpayer's real debts may be deducted from the gross amount of the property. As a rule, no distinction is made between mortgage debts and unsecured debts. Cantons which, like Berne and Fribourg, tax not the whole property, but only parts of it, do not allow deduction of all debts. Berne authorises taxpayers to deduct mortgage debts from the value of real property, but not unsecured debts. If a taxpayer is liable in a canton on only a part of his property, for the reason that the rest of it escapes taxation in that canton, he may only deduct debts to an amount corresponding to the taxable part of his property.

Some cantons prohibit the deduction of debts by taxpayers domiciled or having their head office abroad, in cases when the taxable objects consist exclusively of real property situated in the canton — e.g., Glarus, Grisons, which only allows it subject to reciprocity, Lower Unterwald, Neuchâtel.

Many cantons allow deductions from property ¹.

(b) In cantons which impose a special system of taxation upon companies and co-operative societies, the tax is upon the capital in the business and the reserves. The capital of companies is fixed by their statutes ; that of co-operatives is determined by the balance-sheet. Reserves are generally ascertained by fixing the value of the various assets according to the rules of assessment given above and deducting from this value the amount entered in the balance-sheet.

(c) The explanations given above under (a) and (b) refer also to the communes.

II. Income.

(a) The taxable income is fixed on the basis of a period prior to the fiscal year, which period is usually the preceding twelve months.

In cantons which impose a general income-tax (*cf.* groups I and II, No. 2 (b) (aa) above), the object of taxation is the total net income, which includes the whole of the proceeds and profits, both in cash and in kind, from the labour, industry and activity of the taxpayer, together with the full yield of property and capital belonging to the taxpayer or of which he has the enjoyment. In particular, income includes :

(1) The product of labour and the exercise of a trade or profession, commerce, industry or profit-making enterprise, wages, salaries, bonuses, directors' percentages (*tantièmes*);

(2) Income from copyright and invention patents ;

(3) The proceeds of the cultivation and exploitation of real estate, agricultural land, woods, quarries, mines ;

(4) The yield from the letting and renting of immovable property. Basle-Urban, Geneva and Zurich, for example, add to this the rental value of the dwelling in a building belonging to the taxpayer ;

(5) Annuities, pensions and income from beneficiary interests in real or personal property ;

(6) Income from capital (loans, bonds, cash deposits, dividends, etc.) ;

(7) Profits realised on the taxpayer's property and capital. Basle-Urban also taxes profit that has not been realised.

The net income is arrived at by deducting from gross income the cost of obtaining it (working expenses, rents, salaries and wages, interest on money borrowed), the necessary cost of maintaining the taxpayer's property, reasonable depreciation, and losses in connection with a business.

The product of labour is taxed in cantons which have a special income-tax (*cf.* Groups III, IV and V, No. 2 (b) (aa), above). The income enumerated under Nos. 1, 2, 3 and 5 above is regarded as the product of labour. The cantons of Berne and Grisons do not tax agricultural income. The net yield of labour is obtained by deducting expenses incurred (working costs, rents, salaries and wages, interest on money borrowed), the necessary cost of maintaining the property used in the business whose purpose it is to realise the product of labour, losses in connection with that business and the presumed interest on the capital which the taxpayer has put into his business.

The canton of Berne taxes the income from capital (bonds, deposits, shares, shares in co-operative societies, etc.) by means of the tax on second-class income, but this does not extend to the interest on capital guaranteed by real property situated in the canton.

An increasing number of cantons belonging to the two groups (those with general income-tax and a special income-tax) allow deduction from gross income of sums which the employer voluntarily pays into provident or benefit funds established in the interests of his staff.

Most cantons forbid the taxpayer to deduct from his income or from the product of labour property-tax or income-tax.

¹ For details see the table published on page 34 of Volume 8, *Statistiques de la Suisse*, published by the Federal Statistical Bureau.

No deduction is allowed for the maintenance of the taxpayer and his family. On the other hand, all cantons exempt income up to a given amount or allow abatements varying with civil status and size of the family ¹.

(b) Companies are not taxed on their income, but on net profits, in cantons which have the special system referred to above (No. 2 (b) (bb)). The taxable net profit is that shown by the profit and loss account for the business year preceding the fiscal period. After having eliminated the balance carried over from the preceding business year, the profit is equal to the difference between the gross profit, on the one hand, and the working costs, losses and funds allocated to reserves, on the other hand. Basing themselves on this assumption, the cantonal legislators did not need to authorise companies expressly to deduct these costs, losses and reserves. On the contrary, the cantonal laws provide that to the profit shown by the profit and loss account must be added : sums allocated to reserves or to special funds ; bonuses and percentages distributed to directors and managers ; sums written off in excess of actual depreciation and commercial usage ; and, in general, sums taken from the current year's receipts, before calculating the active balance, in order to meet expenditure that cannot be regarded as working expenses (repayment of capital, acquisition of property).

Geneva and Zurich add to taxable profits the discount on the issue of new shares by the company.

Payments into relief funds for the benefit of the staff may be deducted from profits.

The taxable net profits of co-operative societies formed for purposes of gain are calculated in the same way as those of share companies. Bonuses to customers, who are, as a rule, themselves members of the co-operative, are in many cantons taxed either not at all or only in part.

There are no uniform rules for tax deductions ; sometimes they are allowed, sometimes not.

If the society is only partly liable to tax, the assessment is made without regard to that fact. The tax, however, as thus computed, is reduced in the ratio of the assets liable to cantonal taxation to the total assets of the society.

The rules set forth under (a) and (b) are applied in principle by the communes.

(c) COMPUTATION OF TAX AND ABATEMENTS.

(a) Once the taxable property and income have been determined, the administration fixes the tax quota. To compute this, the taxable income is capitalised and the sum obtained is added to the property, in the cantons of Upper and Lower Unterwald and Vaud.

The law lays down the rate which the administration applies to objects of taxation. These are expressed as fractions of a thousand francs for property and as fractions of a hundred francs for income. The rate for property and income are separate except in the two half-cantons of Unterwald and in the canton of Vaud, which capitalise income. The rates are graduated, except in the cantons of Berne, Schwyz, Upper Unterwald, Solothurn, Schaffhausen and Aargau. These cantons, except Schwyz, substitute for the sliding-scales of the other cantons graduated supplements, which are added to the combined total of the tax on property and the income-tax (see 2 (b) (ee) above). The cantons of Basle (Urban and Rural), Fribourg, Genève, St. Gall, Vaud, Valais and Zurich tax those who are only liable in the canton on a part of their property or income, at a rate corresponding to the total property or income.

The tax quota obtained by multiplying the rates by the amount of the property and income may be called the tax unit. In the cantons of Zug, Fribourg, Basle (Urban and Rural), Ticino,

¹ See pages 34 and 35 of Volume 8, *Statistiques de la Suisse*, published by the Federal Statistical Bureau, which also contains a table of the special abatements granted, instead of working expenses, to persons with fixed salaries and of the deductions allowed to persons in receipt of sickness, old-age and life insurance benefits, etc., up to the amount of the premiums paid.

Vaud, Valais, Neuchâtel and Geneva this unit represents the tax owing to the State. The other cantons fix each year, according to budgetary needs, the multiple or fraction of the unit to be collected. The result of this multiplication gives the tax due for the fiscal period.

The scale of graduation differs widely in the various cantons, and the reader is referred to the table of tax rates published on page 36 of Volume 8 of *Statistiques de la Suisse* (Federal Statistical Bureau).

Except in a few cantons, communal taxes are computed on the same basis as State taxes, but with due regard for differences provided for in the law. The computation is made in the way explained for State tax, the rates applied being those prescribed by cantonal law and in some cases differing from the State rates in that they are either lower or not graduated. The commune fixes annually, according to the needs of its budget, the multiple of the units which it proposes to levy. Communes in the cantons of Geneva and Zurich collect this multiple in the form of a payment supplementing the State tax.

The table published on pages 37 to 40 of the work already mentioned gives the tax rates of the chief town in each canton and of the other larger communes.

(b) No deduction from the taxpayer's quota is allowed under any heading.

6. COLLECTION OF TAX.

(a) BY DIRECT PAYMENT.

The quota being fixed, the demand note is sent to the taxpayer with a request to pay within the time-limit allowed. Payment is always direct, but is more and more made through the post by a payment voucher (*bulletin de versement*) or postal cheque.

According to the canton, payment is effected either all at once or by instalments spread over the year.

(b) BY WITHHOLDING AT THE SOURCE.

The withholding of direct taxes at the source is unknown in Switzerland. However, Federal stamp duties on coupons are withheld at the source (see in this connection the introduction to Part II).

PART II. — METHODS OF TAXING FOREIGN AND NATIONAL ENTERPRISES.

In order that this chapter may be as complete as possible, mention will be made on several occasions of the Federal stamp duties on coupons. It would, however, be a mistake to assimilate these duties to income-tax. By their structure an indirect tax, they bear no relation to taxes on income and property. The Federal stamp duties on coupons are retained by the debtors of the coupons (whether dividend or interest coupons) and paid by them to the tax administration. They are levied by virtue of the Federal law on the stamp duty on coupons, dated June 25th, 1921, as amended on December 22nd, 1927.

A. FOREIGN ENTERPRISES.

I. DEFINITION AND GENERAL PRINCIPLES.

An enterprise which has its statutory seat and centre of management abroad is regarded as a foreign enterprise. An enterprise having its head office in Switzerland is not deemed to be foreign, even if its real centre of management is abroad.

I. *A Foreign Enterprise having no Establishment in Switzerland*, whether the enterprise belongs to an individual, a partnership or a company, is not subject to Swiss taxes on property and income, except in respect of any real estate it may possess in Switzerland. Further, a foreign enterprise interested as member, participant or limited partner in a profit-making concern established in a canton is taxed on its share of property and on its share of income. This participation is treated in the same way as an establishment of a foreign enterprise by cantons that tax the member, limited partner or participant individually (see Part I, 3 (a), Individuals).

II. *Foreign Enterprises having an Establishment in Switzerland.*

(a) Except in a few cantons, the cantonal laws have no detailed rules for the taxation of foreign enterprises having an establishment in the canton. The law lays down the principle ; its application is left to the authorities. In some cantons, the provisions are not even complete, since they only concern property, though this does not mean that the unspecified income lies outside the scope of these provisions. The cantons which have dealt with this matter in some detail are those that maintain close relations with foreign countries, like Basle-Urban, Geneva and Zurich.

(b) Cantonal taxes on property and income are levied upon foreign persons and foreign companies carrying on some permanently established profit-making business in the canton. Examples of such permanent establishments are the head office, the centre of management, branches, factories, workshops, offices, depots, warehouses, agencies and any permanent installation by means of which the foreign enterprise carries on business in the canton. The canton of Berne provides

in Article 17, No. 4, of its law on direct taxes, dated July 7th, 1918, that income-tax is payable independently of length of stay, by all persons who ". . . in any form whatever exercise a trade, industry or commercial business or who possess any income in the canton . . ."

The jurisprudence of the Federal Tribunal in matters of intercantonal double taxation has held for years that an enterprise having its domicile or head office in a canton is liable to income-tax in another canton on whose territory it possesses a permanent material establishment or plant whereby it exercises a qualitatively or quantitatively essential part of its technical or commercial activities. This jurisprudence cannot be applied to cases of international double taxation, but, all the same, it exercises a certain influence even in that field, for it colours the views of the fiscal authorities, who incline to apply it by analogy.

(c) The cantonal and communal taxes are imposed upon property or capital, income, the product of labour or profits, according to the juridical character of the foreign undertaking and the canton in which the establishment is situated.

While the capital invested in the Swiss establishment and the income derived from it are regarded as taxable objects by the laws of various cantons (*e.g.*, Outer and Inner Appenzell, Basle-Urban for individuals, Grisons, Neuchâtel, Lower Unterwald, St. Gall, Schaffhausen, Thurgau and Vaud), other cantons rule that the tax is imposed upon a proportion of the property and income of the whole enterprise (Geneva, Uri, Basle-Urban for share companies formed for purposes of gain). Fractional apportionment is not, however, formally excluded by the laws of the cantons in the first category and may even be said to be normally applied.

The taxable property is not confined to the material elements of the Swiss establishment, such as buildings, machinery, tools, goods and stocks; it also includes rights and claims of the establishment and a proportionate part of any of the capital which may be used as working capital (cash, securities, bank assets, etc.) for the whole enterprise.

The taxable income may be the direct product of the activities of the establishment in Switzerland to which it accrues. Or that establishment may only be contributing indirectly towards producing it and may not receive it at all. In the latter case, the Swiss cantons would still claim tax on part of its income from a foreign enterprise which had an advertising office in Switzerland yielding no revenue¹. Whether the Swiss establishment itself produces income or not, the tax is usually claimed on a proportion of the total income of the foreign enterprise. The question, therefore, whether the income is received or not is immaterial from the fiscal point of view and there seems no need to make the distinction provided for in the questionnaire.

(d) Enterprises belonging to an *Individual*. — An individual domiciled abroad is taxed on the capital invested in the Swiss establishment and on the income or product of labour that that establishment secures for him.

According to the canton in which the establishment is situated, the foreign undertaking is taxed on the net property invested in the establishment in the country or on parts of it, and on the net income or net product of labour that the establishment earns. The cantons of Zurich, Basle-Urban and Geneva, for instance, tax the net property and the net income. Berne subjects immovable property and interest-bearing loans secured on immovable property in the canton to property-tax, the product of labour to the tax on first-class income, and the return of capital bearing interest or yielding a dividend to the tax on second-class income, with the exception of loans already subject to the property-tax.

(e) Enterprises belonging to a *Partnership*. — If the partnership has no legal entity, some cantons tax, not the partnership, but the individual members, according to the rules in force for individuals. The tax is levied upon the part of the property which is deemed to be invested by the foreign undertaking in the establishment situated in the canton. This part is proportional to the

¹ See *Collected Judgments of the Federal Tribunal*, Volume 37, Volume I, pages 356 and 357.

share of the whole property of the enterprise accruing to the person concerned. Income-tax is imposed in the same proportion. This is the rule in the cantons of Zurich, Basle and Geneva, among others.

Other cantons, including Berne, tax the foreign enterprise as such on the property invested by it in the cantonal establishment and on the income which that establishment earns for the partnership. These cantons do not tax the individual partners personally. The partnership's tax is assessed according to the rules applying to individuals, except that the abatements granted to individuals in view of their civil status, the size of the family and economic situation are not allowed or are only allowed on a reduced scale.

A partnership with legal entity is taxed as such. According to the system of taxation in the canton, the tax is imposed on the property invested by the foreign undertaking in its Swiss establishment and on the income which that establishment earns for it, or on a part of the capital (statutory capital and reserves) and of profits. In the canton of Basle-Urban, the tax of the whole undertaking is reduced in proportion to the part of the enterprise carried on abroad. (Section 1, paragraph 3, *Gesetz betr. die Besteuerung der anonymen Erwerbsgesellschaften*, June 23rd, 1921.) Zurich fixes the taxable profits according to the sales figures, taking due account of general overhead; the taxable capital is fixed according to the amount of capital invested in the cantonal establishment. In practice, a fraction of the partnership's total profits is liable for tax (section 33, paragraph 2, *Gesetz betr. die direkten Steuern*, November 25th, 1927). Geneva taxes the partnership on that proportion of its capital and profits which the capital employed in the canton and the profits there earned bear to the total capital and profits (Article 63 of the law on public contributions dated March 24th, 1923). Berne treats legal entities like individuals, and therefore applies to them the rules given above, except that legal entities are not entitled to the abatements granted to private persons in view of their civil status, size of family and economic situation.

(f) Enterprises belonging to a *Company*.—These companies, which have legal entity, are treated in the same way as partnerships having the character of legal entities. Reference may therefore be made to what was said of the latter in the preceding paragraph.

2. TAXATION OF CERTAIN KINDS OF INCOME.

It is assumed that all the special kinds of income about to be considered have their source in Switzerland and that the corresponding capital is invested in Switzerland.

As explained above (Part II, A, 1, II (c)), the property invested by a foreign undertaking in an establishment in Switzerland and the income derived from the latter are among the objects of taxation or serve to determine the proportion in which the foreign undertaking is taxable, whether it belongs to individuals, partnerships or companies. There is therefore no need to distinguish between these different kinds of foreign undertaking in order to decide whether the kinds of income enumerated in the questionnaire are liable to tax or not. Accordingly, the only distinction made is between a foreign enterprise which has no establishment in Switzerland and one that has; the first is designated by a roman I, the second by a roman II.

The income specified in the questionnaire and the capital to which it corresponds are not liable to tax as such, but because they are part of the assessment for taxes of an establishment situated in the canton. In principle, we are concerned in Switzerland with taxes on persons and not on things. The contents of the assessment may vary with the canton, as appears from what was said above on the structure of the tax (Part I, 2 (b) (aa)). In some cantons, there is the further difference due to the special rules applying to share companies and co-operative societies (see Part I, 2 (b), (bb)). Henceforth no express mention is made of the treatment applied to the income or property of a share company formed for purposes of gain with an establishment in one of these cantons. The statement that no tax is imposed covers these companies. When it is said that the tax is

imposed on the income and on the property, it means that these elements are part of the company's profits and capital and are taxed under that heading.

(a) *Dividends.*

In virtue of the Federal law concerning the stamp duty on coupons, a stamp duty of 3 per cent is imposed on share coupons and coupons of beneficiary shares in co-operative societies and on coupons of *actions de jouissance* and *bons de jouissance* issued by a company domiciled in Switzerland. (Articles 3 and 8 of the law mentioned.) This stamp duty is borne by the owner of the security and is deducted from the coupon by the debtor at the time of payment.

I. In the case of a foreign enterprise having no establishment in Switzerland, no direct tax is imposed either on dividends or on the value of securities yielding a dividend.

II. In the case of a foreign enterprise having an establishment in cantons which have a general income-tax and a tax on part of the income, like Zurich, Basle and Geneva, dividends are subject to income-tax. (Groups I and II; see Part I of report, 2 (b).) These cantons further impose the property-tax upon the value of dividend-yielding securities. Cantons which tax the product of labour (Groups III and IV) and the canton of Schwyz only tax the property represented by the share. The canton of Berne only claims the tax on second-class income; including foreign banks having a Bernese branch, but banks exceptionally engaged in the investment of capital do not pay the tax on first-class income in respect of dividends obtained from shares in other companies. Such dividends form part of the gross first-class income (see page 9, Group V).

(b) *Interest.*

(1) *On Bonds.* — Interest on bonds issued by a person domiciled in Switzerland, including those of consolidated bonds (*titres de rente*), mortgage bonds (*lettres de gage*), treasury bonds (*obligations de caisse*), cash and deposit vouchers (*bons de caisse et de dépôt*), is liable to a 2 per cent stamp duty on coupons in virtue of the Federal law on stamp duty on coupons (Articles 3 and 8). This duty is borne by the owner of the security.

I. In the case of a foreign enterprise having no establishment in Switzerland, no direct tax is due either on interest or on the value of bonds.

II. If the foreign enterprise has an establishment in Switzerland, interest and property are treated in the same way as dividends and shares; in the canton of Berne, interest derived from bonds by banks is liable to the tax on first-class and not second-class income, for the reasons given in regard to dividends.

(2) *On Secured Loans.* — The stamp duty on coupons does not extend to the interest on secured loans, except parts of loans secured on real estate in conformity with Article 875 of the Swiss Civil Code and mortgage warrants (*cédules hypothécaires*) and consolidated bonds (*lettres de rente*) issued serially in conformity with Article 876 of the Swiss Civil Code. The duty of 2 per cent is payable by the creditor.

I. No direct tax is imposed on the income from or value of loans, if the foreign enterprise has no establishment in Switzerland.

II. In the case of a foreign enterprise having an establishment in Switzerland, the fiscal treatment is the same as for bonds. Berne, alone among the cantons, imposes property-tax on interest-bearing loans and loans secured on immovable property for their nominal amount. If the security is not situated in the canton, the loan is taxed as an unsecured bond.

(3) *On Unsecured Loans.* — The stamp duty on coupons is imposed at the source on the interest from assets lodged with Swiss banks maturing at more than six months, or the repayment thereof

can only be obtained at six months' notice, and on the interest on loans originating in advances of an amount exceeding 30,000 francs, provided the contractual arrangements guarantee the loan a minimum term of more than two years and on condition that, at any rate, one of the parties is on the commercial register or is commercially engaged in some industry. The rate of the stamp duty is 2 per cent (Article 5 (c) (d), 8 of the law mentioned above), and the duty is payable by the creditor.

I. No direct tax is levied on the income from or value of loans, if the foreign enterprise has no establishment in Switzerland.

II. In the case of a foreign enterprise having an establishment in Switzerland, the information supplied under interest on bonds also applies here.

(c) *Directors' Percentages* (tantièmes).

Directors' percentages distributed by a Swiss enterprise are added to its income or product of labour according to the canton where the enterprise has its statutory seat. Being part of such income or product of labour, these percentages are liable to the tax payable by the Swiss enterprise. The canton of Thurgau does not tax an undertaking having its seat in cantonal territory on the directors' percentages paid by it, unless the recipients of these fees pay tax on them. (Section 16, *Vollziehungsverordnung vom 31. Dezember 1912 zum Gesetze betr. das Steuerwesen.*)

I. The cantons do not claim tax on directors' percentages paid to persons or partnerships situated abroad and having no establishment in Switzerland.

II. Foreign enterprises having an establishment in Switzerland receiving percentages must add them to their taxable income or product of labour. It will, however, very rarely, if ever, happen that an establishment of a foreign enterprise in Switzerland will be in receipt of directors' percentages.

(d) *Royalties for Use of Patents, Copyrights, Trade-marks, Secret Processes and Formulæ and Similar Income.*

I. If the foreign enterprise has no establishment in Switzerland, these are not subject to tax.

II. In the case of a foreign enterprise having an establishment in Switzerland, the royalties mentioned are liable to the tax on income or product of labour if they are collected by the inventor or author. In the hands of heirs or assigns, an invention, an author's works, trade-marks, etc., are regarded as movable capital. This capital is subject to the tax on property and, further, the royalties, if paid periodically, are taxed as income in those cantons which have a general income-tax (Groups I and II; No. 2 (b) (aa), Part I). The canton of Berne imposes only the tax on second-class income.

If the person to whom a copyright is sold exploits the copyright professionally, the sums received are part of his gross income and liable to income-tax or the tax on the product of labour. The copyright sold is part of the purchaser's property, which, except in the canton of Berne, is liable to the property-tax up to its price.

If the person to whom the copyright is sold only collects royalties occasionally, he is liable for property-tax up to the price he paid. Cantons with an income-tax extend the tax to copyright royalties. The canton of Berne imposes on these royalties its tax on second-class income, but not the property-tax.

If the collection of copyright royalties rests with a company or special body, the royalties are considered part of the gross profits of such company or body and are subject to income-tax or tax on the product of labour.

(e) *Rents from Real Estate, Mining Royalties and Similar Income.*

I. In the case of a foreign enterprise having no establishment in Switzerland, cantons with a general income-tax (Groups I and II; Part I, 2 (b) (aa)), including Zurich, Basle and Geneva,

impose this tax on income consisting of rents, etc. They also apply the property-tax to the value of the real estate from which the rents, etc., are obtained.

Other cantons only tax the capital invested in real estate in Switzerland.

The cantons of Inner Appenzell, Glarus, Neuchâtel, Lower and Upper Unterwald, St. Gall, Thurgau, Uri and Vaud do not as a rule allow any deduction of debts from the value of real estate.¹ The canton of Fribourg limits such deduction and the cantons of Grisons and Solothurn only allow it conditionally.

The cantons of Berne, Fribourg, Geneva, Ticino and Valais forbid the deduction of mortgage debts when the creditor is domiciled abroad.

In the case of a foreign enterprise with real property in Switzerland, but no establishment there, some of the cantons which have a special system of taxing share companies and co-operative societies (see Part I, 2 (b) (bb)) tax the real property, not in accordance with that system, but by applying the provisions in force for the taxation of individuals. The cantons in question are Basle-Urban, Geneva, Lucerne, Schaffhausen and Ticino.

II. If the foreign enterprise has an establishment, the imposition is as in the first hypothesis (a foreign enterprise with no establishment in the canton).

All cantons, however, allow deduction of debts secured on Swiss real estate. Fribourg alone limits this deduction, not as an exceptional provision applying to foreign enterprises, but as part of a general rule.

Deduction of mortgage debts in favour of persons domiciled abroad is refused to the same extent as in the first hypothesis and by the same cantons.

(f) *Gain derived from the Purchase and Sale of :*

(1) *Real Estate.* — I. Foreign enterprises having no establishment in Switzerland. In the cantons of Zurich, Lucerne, Zug, Fribourg and Geneva, the profit on a sale of real estate is subject to a special communal tax ; in Geneva alone, the tax is cantonal. The rate of tax is fixed by the communes, except in the canton of Geneva (see Articles 80 to 91 of the law on public contributions dated March 23rd, 1923), which fixed the rate between 10 and 40 per cent.

In the canton of Berne, these profits are taxed as second-class income by the canton and by the communes.

II. Foreign enterprises having an establishment in Switzerland. Cantons which provide for the imposition of a tax either by the communes or by the State in the first hypothesis, do so also in the second. The cantons of Zurich, Solothurn, Basle (Urban and Rural), and Schaffhausen expressly designate as income the profits from transactions in real estate, even when they are not the result of professional activities.

Other cantons tax these profits if they are made by undertakings or persons professionally engaged in the purchase and sale of real estate.

(2) *Securities.* — I. If the foreign enterprise has no establishment in Switzerland, profits are not taxed.

II. In the case of a foreign enterprise having an establishment in Switzerland, profits are taxed as the income or product of labour of an establishment situated in Switzerland, if the establishment buys and sells securities professionally.

The cantons of Zurich, Berne, Basle (Urban and Rural) and Schaffhausen also tax profits on occasional transactions. These profits are added to the establishment's income ; the canton of Berne taxes them as second-class income.

¹ See *Collected Judgments of the Federal Tribunal*, 1928, Volume I, page 75.

(3) *Personal Property*. — I. If the foreign enterprise has no establishment in Switzerland, profits are not taxed.

II. In the case of a foreign enterprise having an establishment in Switzerland, profits are taxed as part of the income or product of labour of the Swiss establishment, if the latter's business is in personal property. If the transaction is only accidental or occasional, no tax is levied. The cantons of Basle-Urban and Berne, however, tax profits in this case also, Basle-Urban including them in the establishment's income, Berne taxing them as second-class income.

(g) *Salaries, Wages, Commissions and Other Remuneration for Services*.

(Note. — The salaries and fees of directors are liable to tax on income or product of labour in the canton where the director is domiciled.)

I. No tax is imposed on these forms of remuneration, in the case of a foreign enterprise having no establishment in Switzerland.

II. If the foreign enterprise has an establishment in Switzerland, salaries, wages, etc., are added to the taxable income or product of labour of the establishment in Switzerland.

(h) *Income from a Trust*.

(Note. — Income of this kind has not as yet played a very important part in the fiscal life of Switzerland, trusts not being common in the country. A more familiar institution is that of *foundations*, created for the management and preservation of capital for some specific purpose — in the interests, for instance, of families. In cases of this kind, the scope of which is inter-cantonal, the Federal Tribunal has held that the cantons are not required to respect corporate *foundations* the only purpose of which is to avoid a heavier fiscal burden and that they are entitled to tax the original owners, if the latter do, in fact, continue to dispose of the corporation's property and if economically they stand in the place of the real party (*Official Collection*, 1927, Volume I, page 440 ; 1929, Volume I, page 373).

If a similar situation arose in the case of a trust, the original owners of the property transferred to the trust under the fiduciary contract would be taxed on the value of the property transferred and, in some cantons, on the income derived from it.

Although, therefore, the trust has no fiscal importance when both the trustee and the *cestui que trust* are Swiss, the question arises whether the procedure would be the same in the case of a *cestui que trust* abroad and a Swiss trustee. We may quote in this connection the judgment given on December 12th, 1930, by the Supreme Commission of Appeal (*Oberrekurskommission*) of the canton of Zurich¹, which decided in favour of the canton that the procedure would be the same. In that canton, therefore, a Swiss trust is not taxed either on the property which it possesses in virtue of a fiduciary contract concluded with a person abroad, or on the yield of such property. The judgment in question admitted the taxation of the trust, not as a matter of principle, but only in the absence of proof to show the real ownership of the property administered.)

I. A foreign enterprise deriving income from a Swiss *foundation* is not taxed personally on that income. It is the *foundation* that is taxed, according to the laws of the canton of its domicile, on the property or on property and income ; the canton of Berne levies only the tax on second-class income, unless the property consists of immovable property within the canton or of capital secured on such property ; these two categories of objects are liable to the property-tax. The jurisprudence of the Federal Tribunal in inter-cantonal cases cannot be invoked.

¹ See issue of October 15th, 1931, *Schweiz. Zentralblatt für Staats- u. Gemeindeverwaltung*, published by Orell Füssli, Zurich ; price of subscription 20 francs.

II. An establishment situated in Switzerland and deriving income from a Swiss *fondation* is personally liable to tax on such income and is also liable to taxes claimed from the foundation by cantons and communes, subject, however, to the note above.

(i) *Income from the carrying on of a Business or Industry through:*

(Note. — The distinction between a foreign enterprise with no establishment in Switzerland and one which has such an establishment does not apply, since this heading deals with other forms of representation.)

(1) *A Local Commission Agent or Broker.* — A broker does not constitute an establishment maintained in Switzerland by the foreign enterprise.

The same applies, generally speaking, to a local commission agent. It may, however, happen that the agent works for the foreign enterprise under conditions which make him the firm's permanent representative. In this case, a number of cantons would tax the foreign enterprise on the property invested in that representation and on the income it earned.

(2) *A Local Dealer or Distributor.* — A monopoly sale of products is not enough to make the place of sale, from the fiscal point of view, an establishment of the foreign enterprise, and the latter is not liable.

(3) *A Travelling Salesman, whether or not having Power to conclude a Contract.* — No tax is imposed.

(4) *A Local Agent with a Power of Attorney.* — By power of attorney is understood the authority to conclude business. If the agent represents a single foreign firm, that firm is taxable on the capital invested in the agency and on the income earned thereby, in six cantons only, among them Berne, which only claims tax on first-class income (excluding real estate), and Zurich; if the agent represents several foreign firms, these firms are taxed by four cantons, including Berne and Zurich. (See *Zürcherische Blätter für Rechtsprechung* 1924, No. 207, Judgment of the *Oberrekurskommission*, Zurich, dated November 24th, 1922.)

(5) *An Agent selling out of a Stock belonging to the Foreign Enterprise.* — The great majority of cantons, including Basle-Urban, Berne and Zurich, but not Geneva, tax the foreign firm on the property invested in the Swiss establishment and on the income it earns, provided the agent represents a single firm. If he represents several foreign firms, the latter are taxed by only thirteen cantons, among them Berne and Zurich, but neither Basle nor Geneva.

(6) *A Permanent Establishment of any Kind.* — In this case, the tax is levied unconditionally by all cantons and all communes on the capital invested by the foreign firm in the permanent establishment and on the resultant income or product of labour. A permanent establishment means in the main the head office, place of management, branches, factories, workshops, offices, warehouses, agencies, depots. A subsidiary company is not, as a rule, regarded as a permanent establishment of the parent company. Nevertheless, Swiss fiscal law does not exclude this possibility, and a subsidiary company may be treated as an establishment of the parent company if the former is completely dependent upon the latter and operates as an organ thereof. (*Collected Judgments of the Federal Tribunal*, 1920, Volume I, pages 175 *et seq.*, Judgment of March 19th, 1920, in the case of *Norddeutscher Lloyd v. Zurich Conseil d'Etat.*) In these circumstances, the subsidiary company is not taxed individually.

B. NATIONAL ENTERPRISES.

1. DEFINITION AND GENERAL PRINCIPLES.

An enterprise is regarded as national if it is domiciled — *i.e.*, has its head office, in Switzerland. The fact that the enterprise may have its real centre of management abroad does not detract from its national character.

(a) A Swiss enterprise is, in principle, taxable on the whole capital that it has invested abroad and all the income it derives from abroad.

One universal exception to this rule relates to real property situated abroad. Here imposition is forbidden to cantons and communes by the jurisprudence of the Federal Tribunal, on condition that tax is imposed by the country where the immovable property is situated.

There is a second, but not general, exception in favour of establishments which a Swiss enterprise maintains abroad. Some of the cantons which grant express exemption in this case do so subject to certain conditions (reciprocity, liability to the foreign tax, etc.). For details, reference is made to Part I, No. 4 (e). It will be noticed that Basle-Urban, Berne, Geneva and Zurich are among the cantons which partially or wholly exempt establishments operated abroad by enterprises domiciled in cantonal territory. To obtain exemption, the establishment abroad must be a permanent installation of some size whose operations represent a substantial part of the activities of the Swiss enterprise.

A third exception is in favour of Swiss persons or enterprises interested as members, participants or limited partners in a profit-making enterprise abroad. This exception, which is less frequent than the second, is formally provided for by the cantons of Basle-Urban (*Ges. betr. die direkten Steuern v. 6. April 1922*, section 14 and section 20) and Berne (*Dekret betreffend die Veranlagung zur Einkommenssteuer v. 22. Januar 1929*, section 5). Zurich also grants exemption, assimilating this participation to an establishment maintained abroad by the Swiss party concerned.

(b) The exception in favour of an establishment abroad relates either to the property invested in the establishment and to the income derived therefrom, or to a proportionate part of the movable capital and income of the enterprise. In relation to share companies and co-operative societies, the exemption applies to a part of the statutory capital and reserves and to a part of profits, in cantons which have a special tax for this class of taxpayer. Among cantons whose laws exempt a fraction of the whole assessment are Basle-Urban (in so far as profit-making companies are concerned), Geneva and Zurich; in the last two, the measure of exemption is such as to leave the canton respectively half and one-third of the total tax. Berne also exempts a proportionate part of the capital and income of the enterprise.

(c) Cantonal legislation furnishes no separate methods of checking the income derived from abroad and the property invested there.

The organs of taxation and appeal have, as a rule, the right to call upon the taxpayer to justify his declaration. In the case of enterprises, the requisite justification usually consists in the production of books, which they are required to keep in virtue of the provisions of the Federal Code of Obligations (Article 877; compare also Article 655 on share companies, Article 701 on co-operative societies). The accounts of a Swiss enterprise must contain the whole of its property and income and thus the capital invested and income derived from abroad.

As already mentioned, these foreign items are, for purposes of taxation, added to the respective Swiss items. There is therefore no need to separate the two and checking is unnecessary, except for real property and establishments exploited abroad. In the cantons which grant no exemption to these establishments, there is no need of check. The taxpayer has to furnish to the revenue authorities, on request, all particulars and any documents that enable them to determine the size of the items to be examined. These authorities may, if necessary, even demand to see the books of the foreign establishment, if any are kept.

A few cantons require the taxpayer to give in his tax return certain details concerning a foreign establishment.

In one case of inter-cantonal double taxation, the Federal Tribunal laid down in an unpublished judgment dated October 12th, 1928, that, failing evidence to show the profits of a branch and therefore of the whole enterprise, the Treasury was entitled to tax the taxpayer *ex officio*. *A fortiori* it will be allowed to tax *ex officio* the property and income of a foreign establishment belonging to a Swiss enterprise, when proof is lacking. In such cases, the empirical method is used.

(d) There is no special method of levying the tax upon capital invested abroad and income derived from abroad, because Switzerland has no special taxes on these items. It is the Swiss enterprise which owes the tax and to which the demand note is sent. This note does not distinguish between the amount of tax pertaining to the Swiss items and the amount pertaining to foreign items.

2. TAXATION OF CERTAIN KINDS OF INCOME.

It is assumed that all the kinds of income enumerated in the questionnaire have their source abroad and that the capital which they represent is invested abroad.

There is no need to consider the taxation of the different kinds of income mentioned in the questionnaire, from the point of view of the three groups of owners — viz., individuals, partnerships and companies. The same kinds of income and property are not, in principle, treated differently according to whether the taxpayer belongs to one or other of these groups. Either they are included in the assessment for tax or they are distributable along with other elements in the same category.

A Swiss enterprise having no establishment abroad is liable to cantonal and communal taxes on almost all the kinds of property and income situated abroad. In order, however, that this statement may be as explicit as possible, a distinction will be made between an enterprise of this kind, which we shall number with a roman I, and an enterprise having an establishment abroad, which will be numbered roman II. It is understood that the income and property belong to the enterprise in Switzerland in case I and to the foreign establishment in case II.

On the other hand, for the reasons explained in the chapter on foreign enterprises (Part II, A, I, II (c), paragraph 4), there would not appear to be any need to distinguish between a case in which the foreign establishment "receives" the income and the case when it does not.

As in Part II, A, 2, no express mention will be made of the taxation of share companies and co-operative societies, unless some special case is met with.

The details given hereunder in connection with the fiscal regime applicable to the various items of property and of income are subject to the explanations given above in connection with the general description of the tax system and the general principles applicable to national enterprises.

In connection with items (a), (b), (c), (f), (g), (h) and inasmuch as they relate to an establishment of a Swiss enterprise, situated abroad (case II), account should specially be taken of what has been said in Part I, under 4 (e) and in the Part II under B 1 (a), second exception. The rules set forth in connection with these items are therefore subject in certain cantons and communes to the restrictions which result from the peculiarities of the taxes of such cantons and communes.

(a) *Dividends.*

The stamp duty on share coupons issued by a foreign enterprise imposed under the Federal law on the stamp duty on coupons does not enter into the question, as these coupons are only liable to the duty when the securities circulate in Switzerland and have been :

- (1) Issued in Switzerland by public subscription or on the basis of a public offer or an offer addressed to a more or less wide circle of persons, or
- (2) Quoted on a Swiss stock exchange.

If these conditions are fulfilled, the duty is generally settled by a single lump sum payment on all the subsequently maturing coupons of securities circulating in the country. The owner of the share does not have his dividend reduced by withholding at the source.

I. In the case of a Swiss enterprise having no establishment abroad, shares of foreign companies are liable to the property-tax except in the canton of Berne.

Dividends come under taxable gross income but not under earnings. Berne taxes them as income of the second class (see Part I, 2 (b)).

II. In the case of a Swiss enterprise having an establishment abroad, the shares of foreign companies are not liable to tax, nor is their yield, subject to the condition, already set forth in the notes at the head of this chapter (Chapter 2), that they are attributable to the establishment situated abroad.

(b) *Interest.*

The remarks in the preceding chapter, concerning the stamp duty, apply *mutatis mutandis* to interest.

I. If a Swiss enterprise has no establishment abroad, bonds and loans, secured and unsecured, are, except in the canton of Berne, liable to the tax on property, and the interest on them to income-tax, but are not liable to the tax on the product of labour. Berne imposes on the interest only the tax on second-class income.

II. No tax is levied on the Swiss enterprise if it has an establishment abroad and if the bonds and debts of foreign debtors belong to such establishment.

(c) *Directors' Percentages (tantièmes).*

I. In the case of a Swiss enterprise having no establishment abroad, the recipient is liable to income-tax or to the tax on the product of labour.

II. No tax is levied on the Swiss enterprise having an establishment abroad, if the latter receives director's fees.

(d) *Royalties for Use of Patents, Copyrights, Trade-marks, Secret Processes and Formulæ and Similar Income.*

(Note. — It is assumed that the royalties here in question have been created or acquired by the enterprise in Switzerland and that that enterprise therefore has the disposal of them. Royalties of this kind are usually payable in favour of the enterprise and not of a dependent establishment.)

I. In the case of a Swiss enterprise having no establishment abroad, income received by an inventor or author is liable to income-tax or to the tax on the product of labour.

The income from patents and other royalties which a person acquires (as heir or purchaser) is liable to income-tax and, further, the capital is liable to property-tax, in the cantons in Groups I and II (see Part I, 2 (b) (aa)). Berne imposes the tax on second-class income.

The income of a person to whom these rights are sold is liable to income-tax or tax on the product of labour.

II. Swiss enterprises having an establishment abroad. Subject to the condition mentioned in the above note, the foreign establishment can only act as the proxy or sometimes as the collector for the enterprise in Switzerland. That being so, the income it earns is attributed to the enterprise in Switzerland and is subject to the treatment set forth under I.

(e) *Rents from Real Estate, Mining Royalties and Similar Income.*

I. No tax is levied on a Swiss enterprise having no establishment abroad.

II. Same observation in the case of a Swiss enterprise having an establishment abroad.

(f) *Gain derived from the Purchase and Sale of:*

(1) *Real Estate.* — The special taxes on profits referred to under the corresponding heading in connection with foreign enterprises do not apply.

I. In the case of a Swiss enterprise having no establishment abroad, no tax is imposed unless the profits are made by enterprises or persons who are professionally engaged in the purchase and sale of real estate. These profits are then subject to income-tax or the tax on the product of labour. The canton of Berne taxes them as income of the second class.

II. No tax is due from a Swiss enterprise having an establishment abroad.

(2) *Securities.* — As regards Swiss enterprises having no establishment abroad, these are treated in exactly the same way as the same class of Swiss property belonging to the Swiss establishment of a foreign enterprise (see Part II, A, 2 (f) (2), II).

II. No tax is due from a Swiss enterprise having an establishment abroad.

(3) *Personal Property.* — I. If the Swiss enterprise has no establishment abroad, the observations on Swiss personal property belonging to an establishment maintained in Switzerland by a foreign enterprise apply here (see Part II, A, 2 (f) (3), II).

II. No tax is due if the Swiss enterprise has an establishment abroad.

(g) *Salaries, Wages, Commissions and Other Remuneration for Services.*

(Note. — The salaries and fees of directors are liable to income-tax or the tax on the product of labour in the canton where the director is domiciled.)

I. Income of this nature belonging to a Swiss enterprise having no establishment abroad are subject to income-tax or to the tax on the product of labour.

II. No tax is due from a Swiss enterprise having an establishment abroad.

(h) *Income from a Trust.*

(Note. — See note attached to the corresponding heading in connection with foreign enterprises (Part II, A, 2 (h)).)

I. Subject to the conditions mentioned in the note, a national enterprise having no establishment abroad, which derives income from a *fondation* or trust abroad, is taxed on such income in those cantons that have a general income-tax; the capital of the *fondation* is liable for property-tax in all cantons except Berne, which imposes the tax on second-class income.

II. No tax is due from a Swiss enterprise having an establishment abroad.

(i) *Income from the carrying on of a Business through:*

(Note. — Here the distinction between a Swiss enterprise which has an establishment abroad and one which has not has no force, since we are concerned with other forms of representation of the Swiss enterprise.)

(1) *A Local Commission Agent or Broker.* — A Swiss enterprise with a broker abroad is not deemed to have an establishment abroad.

The same is true generally of a local commission agent. The reservations made on this point in connection with a foreign enterprise apply here too (see Part II, A, 2 (i) (1)).

Accordingly, the Swiss enterprise is liable to tax on the income derived from the activities of this kind of representative.

(2) *A Local Dealer or Distributor.* — A sales office abroad run by a local dealer or distributor does not constitute an establishment in the sense that the Swiss enterprise would be entitled to claim, from cantons which recognise the principle of exemption, proportionate exemption from property-tax and taxes on income or product of labour in respect of the capital invested in the sales office and the income derived from sales.

(3) *A Travelling Salesman, whether or not having Power to conclude a Contract.* — No fiscal exemption is granted.

(4) *A Local Agent with a Power of Attorney.* — According to the fiscal law and the practice of most cantons, which do not tax the property and income of an establishment outside Switzerland, a local agent with power of attorney, representing a Swiss enterprise abroad, does not constitute an establishment of that enterprise. The latter cannot therefore claim exemption from cantonal and communal taxes proportionate to the size of the establishment abroad, in respect either of the capital invested there or of the income derived from it.

(5) *An Agent selling out of a Stock belonging to the Foreign Enterprise.* — If an agent selling from stock belonging to a Swiss firm constitutes an establishment of that firm, those cantons whose fiscal law provides for the fiscal exemption of such establishments do not impose taxes on the capital invested in the establishment or on the income or product of labour derived therefrom. If the agent represents several firms, his agency is not, as a rule, allowed to count as an establishment of the firms represented. If, on the other hand, he works permanently for a single firm, various cantons accept him as the foreign establishment of that firm.

(6) *A Permanent Establishment of Any Kind.* — A Swiss enterprise which maintains a permanent establishment abroad is exempt from taxes on the property, income or product of labour of the establishment, in cantons that grant such exemption (see Part I, 4 (e)). To obtain exemption, the foreign establishment must be in the nature of a permanent material installation by means of which the Swiss enterprise exercises a qualitatively and quantitatively essential part of its technical or commercial activities. A subsidiary company is not, as a rule, regarded as an establishment of the parent company; Swiss law, however, allows it to be so regarded when the subsidiary is merely an economic organ of the parent company.

PART III. — METHODS OF ALLOCATING TAXABLE INCOME.

1. As far as concerns taxes on property and income, the fiscal laws of the cantons do not as a rule fix the methods of allocating taxable objects. The cantons have been content to embody in their laws the principle of taxing establishments operated in the canton by foreign enterprises and not taxing, or only taxing at reduced rates, establishments operated abroad by cantonal undertakings. The second of these principles, as already stated (see Part I, 4 (e)), does not find universal expression. A few of the cantons, however, have established certain legal rules for the allocation of taxable property and income. Geneva especially, whose law on public contributions contains fairly detailed regulations, makes a distinction between inter-cantonal and international cases of double taxation. Basle-Urban and Zurich have similar though less detailed provisions, Zurich distinguishing between Swiss cantons and foreign countries, Basle-Urban making no such distinction.¹

In the absence of legal provisions, the organs responsible for the enforcement of fiscal laws allocate property and income in cases of international double taxation by applying methods proved by experience and by seeking solutions found satisfactory in inter-cantonal disputes. Frequently the taxpayer tries to arrive at an amicable arrangement, and this is agreed to if the Treasury finds it convenient. Disputes concerning questions of international allocation do not often come before the courts of appeal, falling rather within the sphere of administrative decisions than that of the law. Accordingly, few judgments have been given by cantonal courts dealing with the international allocation of taxable objects, fewer still by the Federal Tribunal.

2. The co-existence in Switzerland — referred to in the introduction to this report — of twenty-five cantons and half-cantons, each with its separate fiscal laws, entails conflicts similar to those arising between a number of foreign countries on whose territory an enterprise operates establishments. Double taxation indeed occurs between cantons, as between one foreign country and another, owing to the diversity of fiscal laws and the fact that the same persons are required by several fiscal sovereignties to pay taxes on the same objects. Still, inter-cantonal double taxation does not present so serious a problem as double taxation between countries. In the first place, there is a certain kinship between the fiscal laws of the different Swiss cantons. Secondly, and more important, the Federal Tribunal, under Article 46, paragraph 2, of the Federal Constitution, not only forbids double taxation as between cantons, but gives the taxpayer the right to appeal to the Federal Tribunal against any infringement of that article. Many cases of inter-cantonal double taxation have come before the Tribunal in the course of years, and its jurisprudence has established certain principles which help the cantons to take the right course, both in the question of fiscal domicile and as regards the allocation of taxable objects. The cantons often apply these

¹ See Basle-Urban, section 1, paragraph 3, Gesetz vom 23. Juni 1921 betr. die Besteuerung der anonymen Erwerbsgesellschaften; Berne, section 6, Dekret vom 22. Januar 1919 betr. die Veranlagung zur Einkommenssteuer, in the wording of the Decree of November 16th, 1927; Geneva, Article 28, paragraph 2, Article 43, paragraph 2, Article 63 of the Law of March 24th, 1923, on public contributions; Zurich, section 11, paragraph 2, section 24, paragraph 2, section 33, paragraph 2, Gesetz vom 25. November 1917 betr. die direkten Steuern.

principles of allocation by analogy to cases of international double taxation, although they are not obliged to do so, as Article 46, paragraph 2, of the Constitution does not cover such cases. Its application, however, offers the cantons the advantage of uniform practice and saves them the trouble of devising suitable rules of their own, which would often be a matter of difficulty.

For the purpose of the present study it would seem well to explain the rules of allocation on which the Federal Tribunal's jurisprudence in the matter of inter-cantonal double taxation is based, the more so as that Court has neither the opportunity nor the power — as regards double taxation between countries — to reconcile divergences existing between cantonal law and cantonal opinion, on the one hand, and foreign law and foreign opinion, on the other hand, as it can in cases of fiscal conflict between two cantons.

Accordingly, a first heading, "Inter-cantonal Cases", in the chapters that deal with allocation methods, will state the principles established by the Federal Tribunal for the allocation of taxable objects between cantons. The judgments of the Tribunal are equally binding upon all cantons, so that there is no need to distinguish between cases in which the enterprise is domiciled in one canton and has an establishment in another and cases in which the position is reversed, in the way that the questionnaire does under A and B for enterprises having their statutory seat respectively in the country and abroad.

3. The Swiss cantons, being members of the same State and bound to each other by close economic ties, have naturally found it convenient and even necessary to make arrangements for lending each other judicial and administrative assistance.

The first of these arrangements, which was embodied in the *Concordat* of February 18th, 1911, concerned the recovery of contributions due under public law and was to the effect that executory decisions and awards by the administrative or judicial authorities of one canton signatory to the *Concordat* should be regarded in any other signatory canton as equivalent to an executory judgment within the meaning of Article 80, paragraph 2, of the Federal law on prosecution for debt and bankruptcy. All cantons have acceded to this *Concordat*¹.

Administrative assistance has not developed far. Some cantons exchange information, spontaneously and on request, on taxable subject-matter and facts of importance for fiscal purposes. The cantonal administrations, however, do not undertake to issue notifications, set on foot enquiries, enter into discussions, collect payments or institute proceedings on behalf of other cantons. The results of expert enquiries carried out by one canton and affecting another canton are not recognised by the latter. Nevertheless, many disputes are settled, with the consent of taxpayers, by agreement between the cantons concerned.

A. FOREIGN ENTERPRISES WITH LOCAL BRANCHES OR SUBSIDIARIES.

I. GENERAL QUESTIONS AND METHODS OF APPORTIONMENT.

(a) BOOK-KEEPING AND ACCOUNTING REQUIREMENTS.

The fiscal laws of the cantons have no provisions which compel the taxpayer to keep books or which require the keeping of books of a special kind. The obligation to keep accounts is laid down in Articles 877 to 880 of the Federal code of obligations, dated July 7th, 1911. There is in this code a further reference to books in Article 655, which requires the management of a share company to provide for the keeping of the necessary books, and in Article 701, whereby the management of a co-operative society is responsible for regular book-keeping.

None the less, the fiscal law of many cantons either entitles the authorities to demand the production of books by the taxpayer or gives the latter the right to produce them in support of his declarations. Share companies, co-operatives and business partnerships are in several cantons

¹ *Official Collection of Federal Laws 1912*, page 611.

required to accompany their tax declarations by copies of their balance-sheets and profit-and-loss accounts. Refusal to submit books is regarded by most cantons as a refusal to furnish the required proof and involves such prejudicial consequences as taxation *ex officio*.

On September 11th, 1925, the Supreme Commission of the canton of Zurich decided in the case of a foreign partnership, having an establishment in the canton, that it was bound to produce the balance-sheet and profit-and-loss account of the whole enterprise¹.

For *Basle-Urban*, provisions concerning the production of books or balance-sheets and profit-and-loss accounts are contained in Article 2, *Gesetz betr. die direkten Steuern vom 6. April 1922*, and in Article 7, *Gesetz betr. die Besteuerung der anonymen Erwerbsgesellschaften vom 23. Juni 1921*; for *Berne*, in Article 27, *Gesetz über die direkten Staats- und Gemeindesteuern vom 7. Juli 1918*; for *Geneva*, in Article 7, paragraph 2, and Article 18 of the Law of December 1st, 1928, amending the Law on public contributions of March 24th, 1923, as amended on December 24th, 1924, March 9th, 1927, and May 4th, 1927; for *Zurich* in Articles 44 and 50, *Gesetz betr. die direkten Steuern vom 25. November 1917*.

The authority responsible for assessing taxes may require the taxpayer to produce any documentary evidence necessary to verify the accuracy of the books submitted.

(b) METHODS OF ALLOCATION.

The method of allocation applied by the Federal Tribunal in disputes arising out of inter-cantonal double taxation is not the same for property as for income. The former is of a particular character and cannot be classed among any of the methods enumerated in the questionnaire. For this reason it will be described first.

Inter-cantonal Cases. — As a rule, each canton is allowed, first of all, to tax items of property localised within its territory. These include land and buildings and personal property, such as machinery, furniture, stores, goods, etc., which are installed on real property. Property of other kinds is apportioned between the cantons concerned in the proportion which the property localised in the canton bears to the total property of the enterprise².

These other kinds of property consist mainly of cash, securities, bank deposits, debts, shares. The distribution between the cantons of these non-localised items of an enterprise's property is not, however, always proportional. In the absence of economic relations with the branches, some of these items are apportioned exclusively to the canton where the enterprise has its registered office or domicile. Thus, in the case of an industrial enterprise the Federal Tribunal decided to allocate to the canton where the enterprise had its seat its shares in other undertakings and permanent advances to subsidiary companies³. In another case of a firm maintaining retail sales stores in several cantons, the Federal Tribunal agreed that there was no direct relation between the securities, cash, debtors, bank deposits of the seat and the retail stores, the latter having no need of working capital. The Court therefore refused to allocate a proportionate share of the assets mentioned to the cantons in which the branches were situated⁴.

The debts of the whole enterprise are deducted proportionately to the property ascribed to the canton. This last rule is subject to exceptions having their origin in cantonal law. In the case of cantons which only tax parts of the property, the deduction of debts can, in principle, only be made in so far as it is provided for by the cantonal law; the same applies in cases when cantonal law allows the taxation of the gross value of real estate and when it is forbidden to deduct any debts at all from the value of the property. The canton of Berne taxes no property except real estate

¹ *Zürcher. Blätter für Rechtsprechung*, 1927, No. 104.

² Cf. *Collected Judgments of the Federal Tribunal*, 1910, Volume I, pages 11 to 20; 1911, Volume I, pages 249 to 260 and 266 to 273.

³ *Collected Judgments of the Federal Tribunal*, 1926, Volume I, pages 247 and 250.

⁴ *Collected Judgments of the Federal Tribunal*, 1924, Volume I, page 178.

and loans secured on real estate situated in the canton ; the owner of real estate may deduct from its value any debts secured on that estate, but may not deduct unsecured debts. In the assessment of communal tax the canton does not allow mortgage debts to be deducted from the value of real estate. The owner must therefore pay the communal tax on the gross value of any real estate he possesses in the commune.

As regards companies and co-operative societies, the method of allocating property explained above results in the taxing of a proportionate part of the corporate capital and reserves, especially in those cantons which tax these legal entities according to a special system. Compare, on this subject, the explanations and examples given hereafter under "Method of Fractional Apportionment" (Part III, A (b), 3, "Inter-cantonal Cases").

International Cases. — In determining taxable property several cantons take exclusive account of objects situated in their territory, but most of them, in accordance with the jurisprudence of the Federal Tribunal described above, assess tax on the localised items of the property and also on a proportionate part of the enterprise's remaining property. Deduction of debts is allowed in the proportion that the gross assets of the branch bear to the total gross assets of the enterprise. This method obtains in the cantons of Basle-Urban, Geneva and Zurich. Berne's method is that described above.

1. *Method of Separate Accounting.*

Inter-cantonal Cases. — The Federal Tribunal does not reject the principle of the direct method of allocating income or the product of labour or profits. If a branch's accounts show approximately the branch's real share of the whole income of the enterprise, allocation may be made on the basis of the separate accounts¹. This may happen when branches are managed as undertakings independent of the central seat, but such cases are exceptional². As the accounts of a branch hardly ever fulfil the condition stated, the direct method is very little used.

It is employed, as will be seen, in the cases of banking enterprises, not directly to allocate profits, but to furnish the comparative data for the distribution of the total profit.

International Cases. — Although a few cantons tax the separate income earned on their territory by the establishment of a foreign enterprise, most assess tax on a proportion of the total income of the enterprise. This majority includes Basle-Urban, Berne, Geneva and Zurich, none of which normally apply the method of separate accounting.

Nevertheless, these separate accounts are of some value in determining the taxable income, because they show the importance of the branch and, provided the books are correctly kept, may furnish certain necessary data for determining the proportion in which the income is distributed between the fiscal sovereignties concerned. Such data are mainly real property, machinery, furniture, stocks of material and goods, wages, turnover. The checking of these data presents no difficulty.

2. *Empirical Methods.*

Inter-cantonal Cases. — The empirical method is not employed to determine income, product of labour or profits.

The empirical method is used as a subsidiary method when fractional apportionment fails in its purpose owing to the absence of accounts or books that establish the profits of the whole enterprise. In the absence of this material, recourse is had to calculation. A percentage is applied to the turnover representing the average profit realised by similar enterprises or the profit is

¹ *Collected Judgments of the Federal Tribunal, 1923, Volume I, page 33.*

² *Collected Judgments of the Federal Tribunal, 1924, Volume I, page 87.*

estimated at that which a similar enterprise of the same size has made. A choice, in fact, is made between such factors as will determine the income by a comparison with other enterprises.

International Cases. — The position is the same as for inter-cantonal cases.

3. Method of Fractional Apportionment.

Inter-cantonal Cases. — The Federal Tribunal has consistently maintained in its jurisprudence that, in the case of an enterprise with establishments in different cantons, the latter could not tax the separate income of the establishments, but only a share of the total profits. This share corresponds to the proportion between the productive factors in the canton and the total productive factors of the enterprise. It may also, according to circumstances, be determined in proportion to working costs¹, turnover² and other elements appropriate to the particular case.

In order to allow for the influence on profits of management and central administration — an influence finding little, if any, expression among the factors of production — the jurisprudence of the Federal Tribunal allows the canton in which the statutory seat is situated to tax a fraction (*pré-impôt*) of the profits, varying from 10 per cent to 25 per cent.

In the cases of industrial enterprises, the factors of production are, on the one hand, localised installations used in production, such as land and buildings, machinery, tools, furniture, motor vehicles, stocks, goods and such assets as cash, securities, debts, etc. and, on the other hand, the labour represented by salaries and wages. The localised factors are allocated to the establishment upon which they depend; the other assets are distributed in their proportion to the localised factors or are ascribed to the establishment upon which they are economically dependent³.

Immovable and movable property is assessed at the value it is assessed at for the property-tax. Salaries and wages are capitalised at 10 per cent⁴ and ascribed to the establishment that pays them. The total figure representing the productive factors in a canton is the numerator of a fraction of which the denominator is the total of all the productive factors of the enterprise. This fraction represents the share of income which the canton concerned may tax.

To avoid misunderstanding, it should be mentioned that the assessments on which the apportionment by the Federal Tribunal is based do not serve for the assessment of cantonal taxes; the cantons determine the value of taxable matter in accordance with their own laws. In a judgment given on June 20th, 1930⁵, in a special case, but one which nevertheless typifies the system, the Federal Tribunal made the following pronouncement:

“ In the case of the *Federal Bank v. the Neuchâtel Conseil d'Etat* the Judgment of January 25th, 1923 (*Official Collection*, No. 49, Volume I, page 33), declares that, as regards banks operating in the territory of several cantons, the separate profit-and-loss accounts drawn up for each establishment of the same enterprise furnish a direct and reliable means of estimating the extent to which each has contributed towards the total net profit, and those profit-and-loss accounts must be the basis for determining the share of profits taxable in the different cantons.

¹ *Collected Judgments of the Federal Tribunal*, 1911, Volume I, page 272; 1914, Volume I, page 214.

² *Collected Judgments of the Federal Tribunal*, 1916, Volume I, page 130.

³ *Collected Judgments of the Federal Tribunal*, 1926, Volume I, pages 246 *et seq.*

⁴ Salaries and wages were for years capitalised at 5 per cent. In a report asked for by the Federal Tribunal, Professor M. R. Weyermann of Berne examined the rate of capitalisation and came to the conclusion that the figure of 5 per cent exaggerated the importance of manual labour as compared with capital. He proposed the rate of 10 per cent, and this was accepted by the Federal Tribunal in its Judgment of November 28th, 1925 (*Official Collection*, 1925, Volume I, pages 40 *et seq.*). At the same time, and on the proposal of the same rapporteur, the Federal Tribunal also decided to capitalise at 10 per cent cost of raw materials, like coal, oils, electricity, while leaving itself full freedom to deal with any subsequent disputes on this matter (for Professor Weyermann's report, see *Revue trimestrielle de droit fiscal suisse*, 1926, pages 1 *et seq.*).

⁵ *Official Collection of Judgments of the Federal Tribunal*, 1930, Volume I, pages 231-233.

“ The plaintiff considers that, once the cantonal share is thus fixed, the cantons are not entitled to calculate in accordance with their own laws the total profits on which they will levy the tax corresponding to their share. In the view of the plaintiff the net taxable profit has to be established according to the same uniform rules that govern the fixing of the shares. And since, for the latter purpose issue premiums (*l'agio d'émission*) are not added to profits, it follows, according to the plaintiff, that, in the case of inter-cantonal enterprises, whenever the shares of the different cantons are reckoned by the direct method, issue premiums cannot be taxed among net profits either in the canton where the enterprise has its central seat, or in the cantons where it has other establishments, although, according to cantonal law, the premiums would be taxable.

“ This absolute solution is inadmissible. The Federal Tribunal has always held that, as regards the taxation of an enterprise operating in several cantons, the fiscal authorities in each canton must assume that the enterprise as a whole is subject to the fiscal sovereignty of the canton. After estimating the taxable profits on this hypothesis — profits which will vary with the fiscal laws of the different cantons — the canton will determine the figure actually taxable, on the basis of the cantonal share as established by the rules of jurisprudence. This principle applies to the assessment of taxable profits and also to the assessment of taxable property. The cantons concerned adopt the shares fixed by the Federal Tribunal and, for the rest, apply the provisions of their own fiscal laws. Article 46, paragraph 2, of the Federal Constitution, which prohibits double taxation, is respected so long as another canton abstains from taxing a fraction of capital or profits in excess of its share (*Official Collection*, 40, Volume I, page 197 ; 41, Volume I, page 437 ; 42, Volume I, page 130 ; 46, Volume I, page 428, etc.). It is true that hitherto the Federal Tribunal has only confirmed this principle in cases when the shares were established by the indirect method (based on turnover or factors of production), but there is no reason for departing from it when the direct method is used (*i.e.*, a calculation based on profit-and-loss accounts, *Official Collection*, 49, Volume I, page 33). A distinction must be made between the establishment of profit-and-loss accounts for purposes of fixing the cantonal share and the determination of total profits for purposes of taxing them on the basis of the share fixed.

“ If, in calculating the shares, disputes arise as to the factors to be included in profit-and-loss accounts, these difficulties must be settled on uniform lines; that is to say, not according to the fiscal regulations of the different cantons, but in accordance with the general principles laid down by the Federal Tribunal. Once the shares are fixed, the position is different. Cantonal law then becomes applicable, and the figure on which the shares are established may not be the same as the figure on which tax is collected at the share rate. Provided that the taxpayer is not taxed on more than 100 per cent of his fortune or income, the Federal Tribunal has no cause to interfere in such cases. If the system proposed by the plaintiff were accepted, it would have the inadmissible consequence that, in the case of inter-cantonal enterprises, a canton would, in the matter of allowing certain amortisation sums, deduction of taxes, etc., treat enterprises differently according as the apportionment was made by the direct method or the indirect method.”

In order to avoid double taxation, the values ascribed by the cantons concerned to the objects of taxation do not need to be the same for the same objects. The double taxation of an enterprise operating in several cantons is avoided as long as the sum of the percentages indicating the cantonal taxation of the enterprise does not exceed 100. Supposing that the Federal Tribunal allowed four interested cantons each to tax 25 per cent of profits, it would be wrong to imagine that there was double taxation just because the income figures taxed in each canton were not the same. The assessment of the enterprise's profits on the basis of the rules in force in the four cantons might result in Canton No. 1 levying tax on an income of 350,000 francs, Canton No. 2 on an income of 300,000 francs, No. 3 on 280,000 francs and No. 4 on 250,000 francs. And yet none of these figures

need exceed the 25 per cent of the enterprise's income as established under cantonal law. *Mutatis mutandis*, the same applies to property-tax.

The principle underlying the system of apportionment becomes clear if we take the case of a company with establishments in four cantons, all of which tax the company on its capital and profits according to its own system, the provisions of substantive law not, of course, being the same.

The following table furnishes an example of apportionment :

Canton	Cantonal taxation		Cantonal share			
	Capital and reserves	Profits	of capital and reserves		of profits	
			%	Amount	%	Amount
A (seat)	12,000,000	1,000,000	33 1/3	4,000,000	40	400,000
B	11,200,000	800,000	22 2/9	2,489,000	30	240,000
C	11,600,000	960,000	22 2/9	2,578,000	15	144,000
D	10,800,000	880,000	22 2/9	2,400,000	15	132,000
			100		100	

The following examples show the working of the principle of fractional apportionment as normally applied by the Federal Tribunal.

Example No. 1. — An enterprise which has its commercial management in one canton (B) and its manufacturing part and technical direction in another canton (A). On April 8th, 1927, the Federal Tribunal decided that profits should be apportioned as follows :

	Total factors of production	Productive factors in canton	
		A	B
CAPITAL.			
<i>Localised factors:</i>			
Manufacture (materials, articles in course of manufacture, etc.)	329,611	329,611	—
Goods	243,338	—	243,338
Machinery and tools.	25,000	25,000	—
Furniture	10,000	5,000	5,000
Plant, utensils, motor vehicles	15,000	15,000	—
Immovable property.	34,800	34,800	—
	657,749	409,411	248,338
	100 per cent	62.2 per cent	37.8 per cent
<i>Other non-localised assets:</i>			
Cash, postal cheques, securities, debtors	145,309	90,433	54,876
	100 per cent	62.2 per cent	37.8 per cent
LABOUR.			
Wages and salaries capitalised at 10 per cent.	803,058	499,844	303,214
	4,770,107	4,121,372	648,735
	5,573,165	4,621,216	951,949
	100 per cent	82.92 per cent	17.08 per cent

Out of the realised profits a fraction amounting to 15 per cent was allowed to Canton B because the importance of the commercial part was not adequately represented by the percentage obtained on the basis of the factors of production, and a fraction amounting to 5 per cent was allowed to Canton A to represent technical management. After deducting the 20 per cent from total profits, 80 per cent remained to be apportioned.

Canton A thus had the right to tax :

$$5 \text{ per cent plus } (0.8 \times 82.92) \text{ per cent} = 71.34 \text{ per cent ;}$$

Canton B :

$$15 \text{ per cent plus } (0.8 \times 17.08) \text{ per cent} = 28.66 \text{ per cent}$$

of the total income of the enterprise. This income is calculated differently by the two cantons, each determining it according to its own law.

Example No. 2. — On May 22nd, 1926, the Federal Tribunal gave a judgment¹ in the case of a large industrial enterprise which has its head office in Canton A, factories working in Cantons A and B, a disused factory in Canton C and goods depots in various cantons. The enterprise is further concerned in certain foreign undertakings. As regards *tax on capital* (property) the various assets were apportioned between the cantons as follows :

1. " Land and buildings, the contents of the industrial inventory, tools, furniture, models and cash " to the value of 19,821,980 francs, were taxable in the place where they were situated.

2. " Raw materials, semi-manufactured products and finished goods " were apportioned according to where these assets happened to be.

3. " Foreign investments (*participations*) " amounting to 24,549,861 francs 45 centimes represented the interests of the company in five foreign enterprises. Investments of this kind are usually subject to the fiscal sovereignty of the canton where the company has its head office. The only exception would be in respect of investments regarded as working capital. In this particular case the taxable company acted as a holding company in relation to its foreign interests, which were accordingly subject to the fiscal sovereignty of the canton where the enterprise had its central seat.

4. " Correspondent accounts (*comptes correspondants*) " to the value of 12,088,725 francs 81 centimes represented permanent or quasi-permanent advances to subsidiary companies and, like the investments to which they are economically directly related, were taxable only in the canton where the company had its head office.

5. " Miscellaneous debtors " amounting to 6,401,779 francs 60 centimes, included assets in the hands of customers, bank credits, etc. The value of this item was allocated between the cantons concerned, excluding cantons in which the enterprise had only depots, and Canton C, where it had a disused factory. Apportionment between Cantons A and B could have been effected either in proportion to the value of the capital thus localised (land, buildings, machinery, plant, tools, cash, raw materials, semi-manufactured and finished goods) or according to quantitative output. These two methods would have given approximately a 50 per cent share to each canton, and the apportionment was, in fact, in this proportion.

6. The value of " securities ", amounting to 211,350 francs, was apportioned in the same way as " miscellaneous debtors ".

¹ *Official Collection of Judgments of the Federal Tribunal, 1926, Volume I, pages 238 et seq.*

Accordingly, the property would be apportioned as follows :

	Canton A	Canton B	Canton C and cantons with depots
	Fr.	Fr.	Fr.
1. Land and buildings, machinery, tools, furniture, cash.	7,268,259	11,546,025	1,007,696
2. Raw materials, semi-manufactured products and finished goods.	6,560,882	5,491,845	630,407
3. Participations	24,549,861.45	—	—
4. Correspondent accounts.	12,088,725.81	—	—
5. Miscellaneous debtors.	3,200,889.80	3,200,889.80	—
6. Securities	105,675	105,675	—
TOTAL	53,774,293.06	20,344,434.80	1,638,103
Proportion	70.983 per cent	26.855 per cent	2.162 per cent

Thus Canton A had the right to tax 70.983 per cent, Canton B 26.855 per cent and the other cantons 2.162 per cent of the total property of the enterprise which would have been liable, had its operations been confined exclusively to the territory of the single canton.

As regards *the tax on the product of labour or profits*, these were apportioned according to the factors of production (capital and labour). The capital factor was determined according to the rules for allocating property for the purposes of the property-tax. The labour factor was fixed by capitalising wages and salaries paid by the enterprise at 5 per cent. The profits were apportioned for tax as follows :

	Canton A	Canton B	Canton C and other cantons
	Fr.	Fr.	Fr.
1. Capital	53,774,293.06	20,344,434.80	1,638,103
2. Labour	89,381,262	60,742,640	4,583,136
TOTAL	143,155,555.06	81,087,074.80	6,221,239
Proportion	62.116 per cent	35.184 per cent	2.700 per cent

Canton A was entitled to tax 62.116 per cent, Canton B 35.184 per cent and the other cantons 2.7 per cent of the total profits or product of labour of the enterprise on which the latter would have had to pay tax in the respective canton, had its operations been confined exclusively to that canton.

Example No. 3. — On October 12th, 1910, the Federal Tribunal ¹, in the case of the *Société Suisse de Pétrole v. Vaud*, gave the following as its reasons for deciding in favour of a fractional apportionment of profits. It further allocated profits in proportion to turnover, a principle which has several times been confirmed in respect of commercial enterprises, notably in a recent judgment of the Tribunal, dated February 14th, 1930.

“In order to estimate the taxable income of an individual or company engaged in trade or industry in several cantons, the fiscal authorities of the canton must take into account the

¹ *Collected Judgments of the Federal Tribunal, 1910, Volume I, page 581.*

Out of the realised profits a fraction amounting to 15 per cent was allowed to Canton B because the importance of the commercial part was not adequately represented by the percentage obtained on the basis of the factors of production, and a fraction amounting to 5 per cent was allowed to Canton A to represent technical management. After deducting the 20 per cent from total profits, 80 per cent remained to be apportioned.

Canton A thus had the right to tax :

5 per cent plus (0.8×82.92) per cent = 71.34 per cent ;

Canton B :

15 per cent plus (0.8×17.08) per cent = 28.66 per cent

of the total income of the enterprise. This income is calculated differently by the two cantons, each determining it according to its own law.

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“ In order to estimate the taxable income of an individual or company engaged in trade or industry in several cantons, the fiscal authorities of the canton must take into account the

¹ *Collected Judgments of the Federal Tribunal, 1910, Volume I, page 581.*

general result of operations, which is the only measure of the taxpayer's resources. Often, too, there would be no way of determining the profits of the various cantonal establishments considered separately, as, for example, in the case of a manufacturing concern involving several distinct operations in different cantons. This difficulty applies to the case at issue. The company buys oil and sells it again; the profit is due both to the price at which the oil is bought and to the price at which it is sold again. All purchases are made in the canton of Zurich, where the company has its head office; accordingly, the gain by the selling branch at Lausanne cannot be estimated apart from the activities of the firm at Zurich. Even when it is possible to determine the profit earned by each establishment, estimates based upon any but the total results of the enterprise would have quite inadmissible consequences. The defects of this method, which are not so apparent when all the branches are making a profit, become glaring when some are working at a loss, and when, in consequence of these losses, the profits of a single branch are found to exceed the final profit of the whole undertaking, as in the present case. The system applied by the authorities of Vaud involves imposing a cantonal tax upon the product of labour of a firm whose accounts in fact reveal a deficit. (It may be mentioned that, as between communes, this system is prevented by an express provision of Vaud law on communal taxation, which lays down that, when a taxpayer carries on his trade or industry in several communes and when the principal establishment or one of the branches shows a deficit, that deficit is deducted from the product of labour of the other branches.)

"Summing up, it is contrary to the principle of the personality of the tax that the product of labour of one and the same person should be split up into several separate and independent products or profits. Just as the person is one, so too is the product of his labour. This may be the result of several factors, but it is impossible to take account of any one of these factors without also taking account of all the others which contribute to produce the final result.

"It may therefore be laid down as a principle that, when a firm has branches in several cantons, each canton is only entitled to tax it on a share of its total income.

"It then only remains to determine by what method the total profits shall be apportioned between the different cantons. The company proposes that they should be allocated on the basis of the turnover figure of each branch of the enterprise — *i.e.*, the number of litres of oil sold in each canton. The canton of Vaud would gain by this arrangement, since this system takes no account of the contribution towards the total profit made by the general management at Zurich. The total profit being 17,886 francs 27 centimes and the turnover of the Lausanne branch representing 12.75 per cent of the total turnover, the Government of Vaud and the Commune of Lausanne may not tax the plaintiff on a product of labour exceeding 2,280 francs 50 centimes."

Example No. 4. — On January 25th, 1923, the Federal Tribunal¹ intervened in the case of a bank operating branches in several cantons. Complaint was made that one of these cantons claimed tax upon a disproportionate share of profits. The Tribunal pronounced as follows on the subject of allocation, which retains its character of fractional apportionment, although based upon the separate profits of the bank's branches.

"It is necessary to consider whether the methods of apportioning profits hitherto adopted in respect of enterprises of another kind (factories or commercial firms — see, among others, *Official Collection* 36, I, Nos. 2, 3, and 94) may also be applied to banks or whether the special conditions under which banks operate do not justify recourse to another method. The question is answered in full detail in Professor Weyermann's report, to which we need only refer. As this expert observes, it is only permissible to resort to indirect methods of calculating the share of the different establishments in the production of the enterprise's total gains, when there is no reliable direct method. As regards banks, however, on the one hand, indirect methods

¹ *Collected Judgments of the Federal Tribunal, 1923, Volume I, page 37.*

(allocation according to importance of factors of production or turnover or established capital) are, for reasons given by the expert, unable to furnish satisfactory results — obviously, two branches of the same bank having the same factors of production, the same established capital and the same turnover may earn very different profits, one even working at a loss, while the other makes gains ; on the other hand, the profit-and-loss accounts drawn up separately for each establishment, offer a direct and reliable means of calculating the contribution of each towards the total net profit. These profit-and-loss accounts should therefore supply the basis of apportionment. There is no question of reverting to a separate examination and taxation of the working results of each establishment. The latter continues to be taxed on a share of the total profits of the enterprise, and the profit-and-loss accounts only serve to determine that share. The difference may not be substantial (subject to a later reference to the share reserved to the canton where the enterprise has its central seat) when all the establishments are making a profit, but it is important when the accounts of one establishment close with a loss. The loss reduces the total profits of the enterprise and will be divided between the other establishments in proportion to their contribution towards those profits.

“ To sum up, the plaintiff's profits taxable in the canton of must be determined, as explained above, from the working results of the establishment as shown by its profit-and-loss account. As the evidence produced does not enable the Federal Tribunal itself to fix the figure for these profits, the cantonal authorities will have to tax the plaintiff anew on the lines indicated. Finally, it should be pointed out that the 10 per cent reserved in the disputed assessment to the canton where the enterprise has its seat (see *Official Collection* 46, I, No. 58) is also justified under the system of apportionment according to profit-and-loss accounts — and this even if the general costs of central administration are divided between the different establishments. The fact remains that, through its direction and control, the central administration helps to earn the profit of each secondary establishment, and the share taxable in the canton concerned should accordingly be reduced by 10 per cent.”

Example No. 5. — An enterprise has three establishments in three different cantons, the management being situated in one of them. One establishment is concerned exclusively with commercial matters, the other two with the manufacture of quite different articles. All three are run as independent enterprises, their autonomy limited only by the powers of the management. On May 12th, 1924, the Federal Tribunal ¹ decided that the profits should be apportioned, not on the basis of sales figures or factors of production, but in accordance with the profits of each establishment, since their profit-and-loss accounts showed with sufficient exactitude the contribution of each establishment towards the total profits of the enterprise. This is not an example of the direct method, but, as in the preceding case, an example of fractional apportionment based on the profits earned by the establishments. The canton in which the enterprise had its centre of management was authorised to tax 10 per cent of the share in profits ascribed to the other cantons.

Having furnished these different examples, we need only consider briefly a few special cases. Companies are in several cantons liable to a further tax on share capital not paid up. This is apportioned in the same way as paid-up capital.

In the case of industrial enterprises, debts, especially debts against purchasers of products and debts resulting from bills of exchange, are regarded, from the economic view-point generally held by fiscal law, as the equivalent of goods sold and belong at least as much to the place of manufacture as to the statutory seat. These debts must therefore be divided equally between the manufacturing establishment and the seat of the enterprise.

Salaries of commercial travellers are ascribed to the commercial part of an undertaking which manufactures its products in one canton and has the centre of its commercial activities in another.

¹ *Collected Judgments of the Federal Tribunal, 1924, Volume I, page 93.*

As regards retail businesses with numerous dependent selling establishments, the assets in the accounts " securities, cash, debtors and similar accounts " belong to the seat of the business and cannot be apportioned between the selling establishments.

International Cases. — The method of fractional apportionment as described above is in use in most of the cantons, including Basle-Urban, Berne, Geneva and Zurich, and the particulars given below refer in the main to these cantons. Geneva, however, has recourse to another method in special circumstances when fractional apportionment of income would fail to meet the fiscal needs of the canton.

The subsidiary of a foreign enterprise is treated as an independent concern. If it operates as an organ of the foreign enterprise, it may be regarded as a branch.

The foreign enterprise is required to furnish all information and produce all documents to enable the fiscal authorities of the canton to establish its total income.

4. *Requirements for Selection of Methods and Value of the Various Methods.*

Neither cantonal law nor the jurisdiction of the Federal Tribunal compels the cantons to employ a given method of allocating the profits of foreign enterprises, but, as already mentioned, most of them do in fact use the method of fractional apportionment.

This method has proved its worth in Switzerland, especially in inter-cantonal relations. It saves the fiscal authorities the corrections necessitated by separate accounting and subsequent appeals by taxpayers ; it allows of a full assessment without surcharge or evasion and it represents the nearest possible approach to fiscal justice. In Switzerland it does not meet with opposition from foreign firms having establishments in the country, as might at first sight be supposed. Although by this method the income of an establishment working at a profit in Switzerland, but depending upon an unsuccessful foreign enterprise, is taxed at a reduced rate or not at all, it does not follow that the fractional apportionment of profits favours the foreign competitor at the cost of national enterprises ; the fractional apportionment of total profits rather avoids this consequence, save in exceptional cases, which may occur rather less often when other methods are used.

(c) APPORTIONMENT BETWEEN BRANCH AND PARENT ENTERPRISE.

(*Note.* — The apportionment of property in the cases enumerated under this heading fully illustrates the general rules given above under A, I (b) of Part III.)

1. *Apportionment of Gross Profits of Local Branch to Real Centre of Management abroad.*

This apportionment is effected by means of the fraction (*préciput*) referred to above in Part III, A, I (b) 3. The size of this fraction will depend on circumstances, and especially on the share of the central management and administration in the control of the business and their contribution towards profits ; it cannot exceed a certain maximum ¹ (25 per cent).

2. *Apportionment of Expenses of Real Centre of Management to Branch.*

Interest Charges.

By the method of fractional apportionment, interest charges are allocated proportionately, like profits, whether they represent debts contracted by the enterprise abroad or by the establishment in Switzerland, and whether the interest is paid by the one or the other.

For purposes of property-tax, interest charges are as a rule allocated proportionally to the gross property ascribed to a State, except in cantons which only tax a part of the property.

¹ Cf. reasons given in inter-cantonal cases : *Collected Judgments of the Federal Tribunal*, 1925, Volume I, page 413 ; 1916, Volume I, page 135.

General Overhead.

What has been said above in connection with interest charges applies also to general overhead expenses.

3. *Apportionment of Net Profits.**Apportionment of Net Profits of Branch to Deficitary Parent.*

The method of fractional apportionment, which is the favourite method in Switzerland and is based on the total profits of the enterprise, requires that the profits of the branch shall be ascribed to the parent, whether the latter is deficitary or not. In practice, the cantons try to mitigate the consequences of this method, which, in the case assumed, deprives them of income-tax, but leaves them the tax on property invested in the branch.

Apportionment of Net Profits of Parent to Deficitary Branch.

Frequently it is not clear whether the branch's deficit is real or fictitious, for it may be the result of arrangements in favour of the parent enterprise abroad. The cantons are all the more inclined towards the method of fractional apportionment.

(d) APPORTIONMENT BETWEEN PARENT ENTERPRISE AND SUBSIDIARIES.

In order that a subsidiary may be assimilated to a branch, it must operate as an organ of the parent company, the two forming a single economic unit. This unity is secured when the subsidiary serves the enterprise as a processing establishment or is at any rate an organ essential to its economic activities. Out of respect for the legal entity of the subsidiary, Switzerland has not hitherto assimilated this subsidiary to the parent company although it reserves the right to alter the results of the subsidiary's accounting for tax assessment, if it is found that the arrangements between subsidiary and parent are plainly in the latter's favour and not in accordance with the ordinary rules and conditions of competition.

The treatment of a subsidiary assimilated to a branch is the same as that explained under (a), (b) and (c); tax is not claimed from the subsidiary as a legal entity, but from the parent company.

II. APPLICATION OF THE METHODS OF ALLOCATION IN SPECIFIC CASES.

(Note. — The allocation of property needs no separate explanation; it accords with the method explained above in Part III, A, I(b), except where some other method of apportionment is expressly mentioned.)

(a) INDUSTRIAL AND COMMERCIAL ENTERPRISES.

I. *Selling Establishments.**Local Establishments selling in National Markets.*

Whether the enterprise manufactures or buys or whether it both manufactures and buys abroad, the method employed to determine the taxable income is that of fractional apportionment.

(a) If the enterprise manufactures abroad, profits are allocated in the ratio of the productive factors abroad to the productive factors in the canton. According to circumstances, a larger or smaller fraction of total profits may be allowed to the central management of the enterprise.

(b) If purchases are made abroad and sales confined to Switzerland, fractional apportionment of profits ascribes a proportionate fraction to general management, the remaining profits being taxed in Switzerland.

(c) If the enterprise both manufactures and buys abroad, profits are apportioned in the ratio of the factors of production. If purchases are of special importance to the prosperity of the enterprise, this fact will be recognised by a larger fraction (*préciput*).

Local Establishments of Foreign Enterprises selling abroad.

Fractional apportionment does not recognise any separate profit made by the establishment situated in the country. However, the sales it effects in a third country increase its importance in relation to the enterprise. The factors of production which have to be ascribed to the Swiss establishment, or its turnover, are more important than they would be if these sales did not take place. The share of total profits accruing to the establishment in Switzerland is so much the larger.

2. *Manufacturing Establishments.*

Profits are fractionally apportioned between the establishment manufacturing in Switzerland and the enterprise selling abroad. Apportionment is on the basis of the factors of production, subject to a fraction (*préciput*) in favour of the seat of management.

3. *Processing Establishments.*

The advantages of fractional apportionment are especially evident in these cases. The Swiss factory shares the profits of the enterprise according to the proportion between its own factors of production and those of the whole enterprise. A fraction is allowed in favour of the seat of management (*cf.* the judgment given by the Federal Tribunal in a case of inter-cantonal double taxation, *Collected Judgments*, 1925, Volume I, page 410).

4. *Buying Establishments.*

A permanent establishment in Switzerland which buys for a foreign enterprise is taxed on a share of the enterprise's profits. According as the foreign enterprise is commercial or industrial, the profits are, as a rule, allocated on the basis of turnover or factors of production, subject again to the fraction in favour of the centre of management.

Since purchases are made on regular terms by a subsidiary established in Switzerland for the account of the foreign enterprise, the latter is not taxed in Switzerland.

5. *Research or Statistical Establishments, Display Rooms, etc.*

Although an establishment in Switzerland does not directly engage in profit-making transactions, it contributes towards the profits of the enterprise. A share of the latter's profits is accordingly allocated to it, provided that it is a permanent establishment.

(b) BANKING ENTERPRISES.

The method of fractional apportionment is also applied to banking enterprises¹. Profits, however, are allocated between the cantons, not on the basis of turnover or factors of production, but on the basis of the profits shown by the separate accounts of each branch. The reason for this is that the branches treat their business as if it were independent. The canton where the central management of the bank is situated is entitled to a fraction (*préciput*) varying according to the importance of the functions exercised by the central management.

The taxable capital of the enterprise is distributed between the cantons concerned, in the proportion which the total assets of the enterprise bear to the assets of the branch.

¹ See *Collected Judgments of the Federal Tribunal*, 1923, Volume I, page 33 ; 1924, Volume I, page 115.

The cantons — in particular, Basle-Urban, Geneva and Zurich — observe the same principles in relations with foreign banking enterprises having branches in their territory ; in the territory of the canton of Berne there are no such branches.

(c) INSURANCE ENTERPRISES.

The fractional apportionment of the profits of a foreign insurance company is effected in the ratio of the premiums of the whole enterprise to the premiums of the establishment operating in Switzerland¹. In one international case profits were apportioned on the basis of the ratio between the premiums of the cantonal establishment and the total receipts of the enterprise².

Property is apportioned on the basis of premiums paid in³.

(d) TRANSPORT ENTERPRISES.

The rules of fractional apportionment applied by the Federal Tribunal in two cases of the inter-cantonal double taxation of railway companies were not absolutely identical. The lines in both cases were of more or less local importance (a suburban line and a mountain railway).

In the one case, the Federal Tribunal on March 27th, 1914, laid down as a principle that the canton concerned was entitled to tax the railway company on a share of its capital and reserves corresponding to the relation between the assets situated in the canton and the company's total assets and on a share of profits corresponding to the volume of traffic in the canton as compared with the total volume of traffic of the enterprise. The factor of "length of line" was rejected as a basis of fractional apportionment because the different parts of the line were of unequal value and traffic was not of equal volume over the whole line. Moreover, account had to be taken of the fact that the seat and management of the company were in another canton.

In the other case, where the tax on profits played no part, the Federal Tribunal on February 28th, 1920, authorised the canton whose claim was the subject of dispute to tax the company on a part of certain assets representing the mean between the share of receipts contributed by the sector operating on cantonal territory and the share represented by the ratio of the length of that sector to the total length of the line. The assets to be thus allocated consisted of rolling stock, stores of material (coal, oil, etc.) and spare parts. The other non-localised assets, such as bank deposits, cash, securities, etc., were considered by the Federal Tribunal to bear very little relation to traffic operations and were for this reason ascribed to the canton where the enterprise had its seat. It may be noted that the line does not appear among the assets allocated. This is because the company was not the owner of the sector situated in the canton (whose taxation was in issue), but operated it as a lease-holder⁴.

In the case of a shipping company⁵, the Federal Tribunal decided that property and income should be allocated between the interested cantons as follows :

Property. — Floating docks, landing-stages and ports, buildings, shipyards, workshops and warehouses ; goods and chattels used for administration, operation and repairs were ascribed to the canton where they were situated ; cash, securities, bank deposits and debtors, to the centre of management, making up a fraction corresponding to the importance of the centre of management ; ships, tugs, stocks of fuel and material necessary for operations were distributed between the cantons in proportion to their share in business activity.

¹ *Monatsschrift für bernisches Verwaltungsrecht*, 1923, pages 143 *et seq.*; Judgments of the administrative Federal Tribunal of the canton of Berne, dated January 8th, 1923.

² *Collected Judgments of the Federal Tribunal*, 1914, Volume I, page 459.

³ *Zürcher Blätter für Rechtsprechung*, 1927, No. 109, Judgment of June 30th, 1926, by the *Oberrekurskommission*, Zurich.

⁴ *Collected Judgments of the Federal Tribunal*, 1914, Volume I, page 76, and 1920, Volume I, page 25.

⁵ *Collected Judgments of the Federal Tribunal*, 1915, Volume I, page 434.

Income. — The balance of income left over after deduction of the fraction for management was to be allocated to cantons in proportion to the importance of the service as reflected in the movement of passengers, goods and luggage.

(e) POWER, LIGHT AND GAS ENTERPRISES.

In the case of an electric power-station on the Swiss frontier having its seat of management in Switzerland, the Federal Tribunal by analogy applied Article 46 of the Federal Constitution prohibiting double taxation as between cantons. The installations in the other country and the income earned there were exempt from cantonal and communal taxation¹.

In order to take account of the activity which produces electric current — which would otherwise have been left out — the Federal Tribunal, by a judgment of December 22nd, 1926, allocated the income, not on the basis of receipts from the territory of the cantons concerned or of current consumed in that territory, but on the basis of the factors of production (capital and labour).

(f) TELEGRAPH AND TELEPHONE ENTERPRISES.

No examples can be quoted, telegraphs and telephones being run by the Confederation.

(g) MINING ENTERPRISES.

In the case of the Travers asphalt mines, belonging to a British company, the canton of Neuchâtel taxes the Swiss undertaking, not on the basis of the capital assets invested in the mines and on the share of total profits accruing to those mines, but by a flat contribution fixed per ton of asphalt extracted. There is no other example to quote.

B. NATIONAL ENTERPRISES WITH BRANCHES OR SUBSIDIARIES ABROAD.

I. GENERAL METHODS OF ALLOCATION.

Reference must first be made to the statement of legal provisions contained in Part I, Section 4 (e).

Among cantons which remit part or all of the taxation of foreign branches or subsidiaries of national enterprises are Basle-Urban, Berne, Geneva and Zurich.

Basle-Urban, Geneva and Zurich apply the method of fractional apportionment; Geneva and Zurich in every case levy a given part of the tax which the enterprise would have to pay if it were liable to tax on the whole of its property and income. Geneva has fixed this part at one-half, Zurich at one-third, both for property-tax and income-tax, and both for cantonal and for communal taxation. Berne grants certain variable abatements; the *Conseil d'État* decides their extent in the light of the circumstances of each particular case. This system does not, of course, adhere to any given method of allocation.

Foreign subsidiaries are not, as a rule, treated as branches of the national enterprise, but the cantonal authorities reserve the right to consider whether the Swiss parent firm grants the subsidiary company advantages which really amount to a surrender of profits. If it is so, the accounts of the national enterprise are adjusted.

¹ *Collected Judgments of the Federal Tribunal, 1920, Volume I, page 417.*

II. ALLOCATION OF PROFITS TO REAL CENTRE OF MANAGEMENT WITHIN THE COUNTRY.

A fraction of the total profits of an enterprise is ascribed to the seat of the enterprise, which usually coincides with the real centre of management.

This fraction is a fixed percentage of the total profits. The figure depends on circumstances ; it will be larger or smaller according as the functions of the seat are of more or less importance to the enterprise. As a rule, it is not less than 10 per cent and not more than 25 per cent.

C. HOLDING COMPANIES.

I. SWISS HOLDING COMPANY CONTROLLING ONE OR MORE FOREIGN SUBSIDIARY COMPANIES.

In many cantons, holding companies enjoy privileged treatment as compared with other companies. This treatment is granted impartially to companies participating in Swiss subsidiaries and companies participating in subsidiaries abroad. Companies treated as holding companies are share companies and, in several cantons, co-operatives and even associations whose purpose consists in participation in other enterprises and whose profits are derived from subsidiaries. The law of some cantons demands that such participation shall be the holding company's exclusive aim, while others only insist that it shall be the chief aim.

The fiscal privileges vary with the canton. Some grant a reduction of the normal tax, others apply a reduced rate to the capital and do not tax profits.

The table attached to the present report supplies the requisite data to show the treatment applied to holding companies by those cantons which grant them privileges.

II. SUBSIDIARY COMPANY ESTABLISHED IN SWITZERLAND CONTROLLED BY A FOREIGN HOLDING COMPANY.

The Swiss subsidiary is in principle treated as an independent company. There are, however, possible exceptions ; one was given above in the chapter dealing with allocation between parent and subsidiary (Part III, A, I(d)).

Annex.

TARIFF OF TAXES.

I. CANTONAL TAXES ON INDIVIDUALS.
(Figures applying to the tax year 1930.)

Cantons	Rate of tax fixed by the law		Multiplier of the legal rates as fixed by the competent authorities
	On property (per mille)	On income (per cent)	
Zurich	1.5 -2.5	1-6 (progres. scale 1-8)	1
Berne	1	Ist Cl. 1.5 IInd Cl. 2.5	3 ¹
Lucerne	1.5 -2.2	0.2 -4	1
Uri	1 -4	0.6 -5	1
Schwyz	1	1 ²	2½ ²
Upper Unterwald	1	0.5 -1.5	1 ³
Lower Unterwald	1 -1.3	0.4 -0.6	1.5
Glarus	1	1	2½ ⁴
	1 ⁵	—	0.5 ⁵
Zug	2.25-4.50 ⁶	2.25-4.25 ⁶	—
Fribourg	2 -4.8	0.6 -4.8	—
Solothurn	0.5	1	1½ ⁷
Basle-Urban	1 -6	0.5 -12.5 ⁸	—
Basle-Rural	1 -4	0.5 -6.5 (0.5 -3.2)	—
Schaffhausen	1	1	2 ⁹
Outer Appenzell	1 -1.25	0.1 -1	1½
Inner Appenzell	1 -1.3	0.2 -0.8	5½
St. Gall	1 -2.5	0.4 -2	2½

¹ Five per cent of which represents the poor rate. The taxes whose total (excluding the poor rate) exceeds 100 francs are increased by 5 to 50 per cent.

² Only applies to life annuities and pensions.

³ When the basic amount of tax exceeds 70 francs, it is increased by 5 to 25 per cent.

⁴ The amount of income-tax (which applies only to the yield of labour) is increased by 10 to 250 per cent. In addition to the annual property tax of 2.5 per mille, a supplementary tax, which goes from 0.1 to 2.5 per mille is collected.

⁵ School rate. The basic amount of tax is increased by 5 to 125 per cent.

⁶ These rates are the legal rates as increased by the competent authorities.

⁷ The basic amount of tax which exceeds 20 francs is increased by 10 to 100 per cent.

⁸ This rate only applies to the commune of Basle. In the suburban communes, the rate goes from 0.25 to 6.25 per cent.

⁹ The basic amount of tax which exceeds 20 francs is increased by 5 to 100 per cent.

Cantons	Rate of tax fixed by the law		Multiplier of the legal rates as fixed by the competent authorities
	On property (per mille)	On income (per cent)	
Grisons	I -2	0.4-4.2	2.5
Aargau	0.3 -I.2 ¹⁰	I	2 ¹¹
Turgau	I -2	0.3-I.5	2½
Ticino	2 -8 ¹²	0.5-10 ¹²	—
Vaud ¹³	I.5 -8.5	I.5-8.5	—
Valais	I -6	I -7	—
Neuchâtel	I.6 -7	I.I-7	—
Geneva	I.75-4	I -8 I -10.2	—

¹⁰ Capital assets and goodwill, 1.2 per mille; lands 0.8 per mille; buildings, 0.6 per mille; furniture, 0.3 per mille.

¹¹ The basic amount of tax which exceeds 40 francs is increased by 5 to 70 per cent.

¹² There is also a supplementary tax of 10 per cent which is collected on behalf of the school.

¹³ The amount of tax assessed is reduced by 4 per cent.

II. CANTONAL TAXES ON COMPANIES (SOCIÉTÉS ANONYMES) AND PROFIT-SEEKING CO-OPERATIVES¹
(SOCIÉTÉS COOPÉRATIVES A BUT LUCRATIF).
(Figures applying to the tax year 1930.)

Cantons	Rate of tax fixed by the law		Multiplier of the legal rate
	On capital (per mille)	On profit (per cent)	
Zurich	I.5	-10 ²	I
Berne	I ³	Ist Cl. I.5 IIInd Cl. 2.5	3 ⁴
Lucerne	I	-8 ²	I
Uri	I -4	0.6-5	I
Schwyz	I	—	2½
Upper Unterwald	I	0.5-I.5	I ⁵
Lower Unterwald	I -I.3	0.4-0.6	I.5
Glarus:			
Ordinary tax	I	I ⁶	2½
School tax	I	—	0.5

¹ Many cantons apply special rates to certain categories of co-operatives — e.g., consumers' co-operatives.

² Half of the percentage which net profit represents towards the taxable capital.

³ Capital = Real property and debts guaranteed by mortgages which produce interest.

⁴ The canton collects an additional tax of 5 to 50 per cent of the total amount of taxes other than the cantonal poor tax, if the amount of these taxes exceeds 100 francs.

⁵ The amount of tax which exceeds 70 francs is increased by 5 to 25 per cent.

⁶ The basic amount of tax due on profit which exceeds 6,000 francs is increased by 10 to 250 per cent.

Cantons	Rate of tax fixed by the law		Multiplier of the legal rate
	On capital (per mille)	On profit (per cent)	
Zug	2.25-4.5 ⁷	Fr. 4-20,000	—
Fribourg	1.5 (0.75) ⁸	3 -8 ²	1
Solothurn	0.5	1	1½ ⁸
Basle-Urban	2 (0.5) ⁸	-12 ²	—
Basle-Rural	1.2 -2 (0.6-1) ⁸	-10 ²	—
Schaffhausen	2	3 -12 ²	1½/7
Outer Appenzell	1-1.25	0.1-1	1½
Inner Appenzell	1-1.3	0.2-0.8	5½
St. Gall	2.5-3.5	5 -15 ¹⁰	—
Grisons	1-2	0.4-4.2	2½
Aargau :			
Ordinary tax.	1.2	1 ¹¹ 1 ¹²	2,
Special tax.	1.2, 0.25 ¹³	—	—
Turgau	1 ¹⁴ , 1-2 ¹⁵	0.3-1.5	2½
Ticino	2 ¹⁶	-10 ² 16	—
Vaud	1.5	-8.5 ²	1½
Valais	1.5 (1) ⁸	-12 ²	1
Neuchâtel	1.6-7	1.1-7	—
Geneva	1.5 (0.75) ⁸	-13 ¹⁷	—
„ (special tax on buildings) ¹⁸	11½-2	—	—

⁶ Half of the percentage which net profit represents towards the taxable capital.

⁷ These rates include, in addition to the legal rates, those fixed by the competent authorities.

⁸ The figures in parentheses apply to unpaid capital.

⁹ An additional tax of 10 to 100 per cent is collected when the amount of the normal tax exceeds 20 francs.

¹⁰ The percentage of the tax is equal to the percentage which the profit represents in relation to the taxable capital.

¹¹ Dividends and directors' percentage.

An additional tax of 5 to 70 per cent is collected when the basic tax exceeds 20 francs.

¹² On interest-bearing loans.

¹³ Real property.

¹⁴ Goodwill.

¹⁵ A supplementary tax of 10 per cent (cantonal school-tax) is collected.

¹⁶ Sixty-five per cent of the percentage which the profit represents in relation to the registered capital.

¹⁷ The tax varies according to the destination of the buildings and the object which the company pursues.

III. HOLDING COMPANIES (SOCIÉTÉS DE PARTICIPATIONS).
(Figures applying to the tax year 1930.)

A. Cantons collecting only a Part of the Ordinary Amount of Tax.

	Canton	Commune
Aargau.	one-quarter (real estate excepted) evaluation	the half (real estate excepted) Government evaluation
Fribourg	evaluation	Government evaluation
Lucerne.	up to one-quarter	up to one-quarter
Lower Unterwald	evaluation	evaluation
Upper Unterwald	evaluation	evaluation
Solothurn.	one-fifth	according to communal regulations
Vaud.	one-quarter	one-quarter

B. Cantons having Special Tax Rates.

	Canton	Commune
Basle-Urban.	{ 1 per mille of paid-up capital 1/4 per mille of unpaid capital	— —
Basle-Rural.	{ 1/2 per mille of paid-up capital 1/4 per mille of unpaid capital	1/2 per mille of capital 1/4 per mille of capital
Geneva.	{ 1 per mille of paid-up capital 1/2 per mille of unpaid capital	additional centimes —
Glarus	4/10 per mille of capital	—
Grisons.	1/2 per mille of capital	—
Neuchâtel.	1 per mille of capital	1 per mille of capital
St. Gall.	1/2 per mille of capital	1 per mille of capital Ordinary tax on real estate — <i>i.e.</i> , on the rental value of the property
Schaffhausen	1/4 per mille, of which at least the half goes to the commune	—
Ticino	4 per mille, of which half goes to the commune	—
Valais	1/2 per mille of capital	ordinary tax on capital and income
Zug	1/2 to 1 1/2 per mille, of which half goes to the commune	—
Zurich	1/2 per mille of capital	additional centimes

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