"The foregoing provisions do not apply to fees paid to the managing directors or directors in excess of the sums allocated to other members of the board of directors, or to the sole manager, in so far as these constitute remuneration for their work of management, with the reservation that in each company not more than two managers, designated by name, may, avail themselves of the provision.

(v) On attendance paid to shareholders of companies on the occasion of general meetings.

(vi) On redemption premiums paid to creditors and on lottery prizes paid to bondholders."

(c) The physical location of the notes or security is immaterial.

(*d*) *Idem.*

(*e*) *Idem.*

(f) Article 6 provides that "When an Egyptian joint-stock company has received registered shares or participations as consideration for contributions in kind or in cash made by it to another joint-stock company, Egyptian or foreign, the dividends distributed by the first company shall in each finacial year be exempt from the tax on income investments established by Article, 1 of the present law, in so far as they represent the yield derived by it from these shares or participations during the financial year, provided that the said shares and participations remain in the company's name and that the yield thereon has paid the tax on income from transferable securities".

(2) No.

(3) *Idem.*

(4) *Idem.*

(5) *Idem.*

(g) **Income from royalties on patents, trade-marks and other commercial or industrial properties**

These are not subject to any income-tax.

(h) **Income from royalties on copyrights and other intellectual properties**

Idem.

(j) **Private pensions and annuities**

Article 61 provides that a tax shall be levied on salaries and similar income and pay, allowances and pensions, (L. Articles 1, 15, 30, and 72), including

(1) All salaries and similar income, pay, allowances, emoluments, wages, pensions and annuities paid by the State or the provincial councils, to any person resident in Egypt or abroad, without prejudice to agreements providing for exceptions.

(2) to salaries and similar income, pay, allowances, emoluments, wages, pensions and annuities paid by all banks and campanies or by private individuals to any person resident in Egypt, or to any person resident outside Egypt, for services rendered in that country (L. Articles 1, 4, 30, 72 and 75—R. Articles 33 and 38).

The tax is payable on any sum of money due under this head for the period beginning on the first of the month following promulgation of the present law. (L. Articles 1, 17, 28, 30, 72).

(k) **Earned income from personal services, private employment or liberal professions (fees, wages, salaries)**

(1) See Article 61.

(2) *Idem.*

(3) *Idem.*

(4) *Idem.*

II. CAPITAL GAINS TAX

There is no such tax.

III. CAPITAL AND PROPERTY TAXES

There are no taxes on capital or property.

IV. SUCCESSION AND GIFT TAXES

(a) (1) The tax is assessed separately on the net share of each beneficiary (Law No. 142 of 1944).

(2) As a general rule, on estate plus gifts *mortis causa* and gifts *inter vivos* to heirs, provided that the gifts were made within a year preceding decease.

(3) The tax is levied on the domestic assets of the estate or *ab intestat*, and on the domestic items of the gift as described in paragraph 2 exclusively.

(4) The tax is levied :

"1. on any property whether movable or immovable left by an Egyptian, whether the *de cujus* was resident in Egypt or abroad ;

2. on any real property situated in Egypt, even where the *de cujus* was a foreigner, wherever his domicile may have been ;

3. on movable property situated in Egypt and left by a foreigner whose legal domicile was in Egypt or who had exercised a profession or exploited property in that country."

(b) (1) See the answer to the preceding question.

(2) *Idem.*

(3) No rules beyond those already noted.

(4) *Idem.*

(c) (1) Article 1 of Law 142 of 1944 provides that the tax is payable in accordance with the following scale :

On the share of the descendant's spouse, father and mother the duty is :

2 per cent on the first	£	5000	Egyptian	
3 per cent on the next	£	5000	,,	
4 per cent on the next	£	5000	,,	
5 per cent on the next	£	5000	,,	on the heir's
6 per cent on the next	£	10000	,,	net share
7 per cent on the next	£	10000	,,	
8 per cent on the next	£	10000	,,	
10 per cent on any sum in excess of these.				

Any heir in the above categories whose net share does not exceed £ 500 Egyptian is exempted from duty ; if the share exceeds this sum, the exemption will still apply to the first £ 500 Egyptian; if it exceeds £ 4000 Egyptian, duty is payable on the whole share. The duty is doubled for ascendants, with the exception of the father and mother and for brothers and sisters, and is trebled for nephews and other collateral relatives to the fourth degree, and quadrupled for all other heirs. No exemption is granted to heirs in the various categories in respect of the amount of their share in the estate.

(2) See preceding paragraph.

(3) There are no differences in the method of collection.

V. CAPITATION AND HEAD TAXES

There are no such taxes.

V. REPORT OF THE COMMISSION ON TAXATION OF THE INTERNATIONAL CHAMBER OF COMMERCE (February, 1965)

Exemption Vs. Tax-Credit Method

*** *** ***

II. THE CLAIMS OF THE COUNTRY OF RESIDENCE AND OF THE COUNTRY OF ORIGIN

The country in which the investor resides is the country which provides the capital in international investment : for the purpose of this study that country will be described as the country of residence. The country in which the enterprise or the borrower of the funds is situated is the country where the income originates which is generated by the capital : for the purpose of this study that country will be described as the country of origin.

The progress of thought on the at times conflicting claims of these two types of country has developed gradually under the influence of economic change. In the days when the countries which had capital to supply to others were practically alone in enforcing income taxes on their subjects, it was seriously argued that they had the first claim to tax income earned in a foreign country on the capital they provided. The thought was that if the country in which the capital was invested charged a tax on that income, the supplier of the capital was entitled to, and did, put back that charge by increasing the price of his service to cover the tax. Therefore, the countries in which the income originated should yield to the inevitable and exempt the income which arose in its country to the non-resident.

That reasoning is scarcely now defended in government circles. It is generally admitted that the country in which the income arises has the first claim to tax that income. The country in which the owner of the income resides must come

second—if at all. The challenge which now comes from the capital-seeking, or under-developed countries is that the country in which the income arises has the sole right to tax that income. They claim that the enterprise belongs to their economy and that if they have fixed a rate of tax on profits which is the most that can be paid if the enterprise is to remain financially sound and able to develop itself and the country, it is wrong for the country of residence to impose an additional tax on those profits which will or may prevent the enterprise from developing. They want the profits which remain after taxation to be re-invested in the country after paying a reasonable return to the investor, and they resent the country of residence extracting part of those profits by means of an additional tax.

Countries which are under-developed by comparison with industrial countries with a high standard of living are seeking the help of those countries in their task of self-improvement. The leading countries of the western world have accepted this moral claim to their assistance. The incidence of taxation is relevant in this context, because private capital cannot be driven but must be attracted to investment in under-developed countries. Grants-in-Aid and the provision of loans at low rates of interest are the appropriate method of providing help from government to government. Private capital is attracted by the relative yield after tax. Tax may be imposed in the country of residence in addition to tax in the country of origin. Some countries of origin which are under-developed countries suggest that the countries of residence should reduce their taxes on income derived by their residents from the under-developed countries, so that in total, including the tax imposed by the country of origin, the tax is less than it would have been on income originating at home. Without adjudicating on this claim, for the under-developed countries also have an obligation to moderate their taxes if they desire to attract capital, it is sufficient for the moment to record that the tax policy of the capital-supplying country should be consistent with its decision to help the under-developed countries. If its tax laws are an impediment to the flow of private capital to the under-developed countries, those laws should be re-examined. Exemption of foreign income is consistent with the decision to assist the under-developed countries.

III. EXAMINATION OF THE CLAIM OF THE COUNTRY OF RESIDENCE

(a) The Right to Tax the Total Income of Residents

The country of residence of the investor usually has a progressive rate of tax which increases with the increase in size of the total income, in order to reflect the ability of the tax-payer to contribute to the common expenses of the State. It contends that all residents should be treated alike regardless of the differences in character of their total income. There should be no discrimination for or against particular classes of tax-payers or particular classes of income; all should pay by reference to their total income.

This argument appears to be weighty at first sight, but weakens considerably on closer examination. If it is true at all, it can only be true in relation to that part of the total revenue which is collected by means of propressive taxes. It is not true of proportional taxes on income. It is completely out of place in considering indirect taxes on consumption or on turnover.

The proportion of the total revenue which is collected by means of progressive taxes based on total income differs in each country. Nowhere is it more than half, and in most countries it is less than half, of the total revenue. Therefore it is an exaggeration to elevate the idea of taxing according to ability to pay into a principle which must be preserved at all costs.

In most countries the different types degrees and of severity of taxes are designed to achieve a certain economic result. Considerations of logic are mixed with considerations of expediency and of practicability. Not all income is of the same type or even toughness. Some types wither away more quickly

than others when the amount taken by the State is increased. It is not practical to treat all income as being alike.

It would not be disputed that income derived from foreign sources is less tough than income from home sources. This is true even of income arising in settled countries at a mature stage of development. The non-resident is at a disadvantage compared with the resident. Even if he were not at a disadvantage and only thought that he was, that state of mind would be sufficient to induce him to dispose of his foreign source of income in favour of a home source if some trouble appeared to threaten.

Even on the narrow ground of logic, the country of residence cannot carry its argument of equal treatment of foreign income with home income to its logical conclusion. For in a case where the foreign tax levied on the foreign income is greater than the home tax payable on the same income, the country of residence should pay the recipient a sum equal to the excess of the foreign tax, in order to equalize him with his fellow citizen who had the same amount of income from home sources.

It is not seriously suggested that such a payment should be made. The illustration is drawn only to demostrate that the argument, which at first sight appears to be based on equity between taxpayers, turns out to be a pure revenue-collecting argument that the resident should pay the foreign tax or the home tax whichever is the higher on his foreign income.

(b) Tax to be Paid for the Benefits of Residence

The country of residence claims to tax foreign income of its residents, because it provides a residence for them, namely the peace, order and amenities which the resident desires. It also claims to tax income which arises in the country and belongs to non-residents, on the ground that it has created the conditions in which the income could be procured. No one disputes the latter claim; it is the claim of a country of origin. The first claim, however, rests on a different ground and needs to be more closely examined before it is admitted. The country of residence admits that it has no hand in producing the foreign income apart from the argument of control; it claims to have given protection and amenity to the resident person to whom the income belongs.

In the case of an individual, it is possible to draw a distinction between taxes on the income and taxes on consumption. Practically every country in the world has both. If the moral right of the State to levy taxes depends on the services which the State provides, and if in the case of foreign income the State has practically no influence on the production of the income, whereas in the case of amenities to the person the State does enable them to be provided under its government, it would seem a fair demarcation of rights if the State levied no income-tax on the foreign income but was entitled to the taxes paid by the resident individual on his consumption.

In the case of a company which is created under its laws, the State is entitled to a contribution for giving a legal personality to the company. This contribution is normally in the form of stamp duty or registration duty. If the company is carrying on business abroad, the State of residence of the Company can have a moral claim to a tax of those profits, if the business has its effective head office in that country, inasmuch as it provides a home for the brain of the business. Where, however, the effective management of the business is also abroad, the only activities which are done in the country of residence are formalities connected with the compliance with the law relating to the conduct of companies. The consideration, which was once present, that a government could protect its nationals in another country, has not the validity which it once had. The jurisdiction of the country where the income is earned and the capital is invested is overwhelmingly predominant.

From this line of thought, the country of residence may have a moral claim to levy a personal tax on a resident individual in respect of his foreign income, which is considerably less than the tax levied on income arising inside its jurisdiction to a resident. But it could be contended that the indirect taxes on consumption which the resident pays are sufficient to discharge his obligation.

In the case of a company, there may be a moral claim to levy some tax on the foreign profits if the real seat of management is situated in the country of residence, but the claim dwindles to vanishing point the greater the degree of control exercised in the country of origin.

(c) Business Profits said to be earned at the Seat of Control

Another argument is based on a contention that profits are earned at the place where the control of the business is situated. If the business is deemed to be resident in a country because the management and control is situated there, then *ipso facto* the profits, it is said, must have been earned there and not in the country where the enterprise is situated.

This argument runs counter to the principle of all double taxation agreements, whether they are model agreements or actual agreements, whereby profits of an enterprise are deemed to be earned where the enterprise has a permanent establishment and the amount of the profit is to be determined by assuming that the transactions of the permanent establishment with its head office are done on the terms which would obtain between independent persons transacting business on an arm's length basis.

(d) Migration of Capital

Still a fourth argument by a country of residence is that if its general rates of tax are higher than the rates of tax levied in the country where the income arises and if foreign income is exempted from the home tax, residents will be tempted to sell their investments in the home country and to remove their capital abroad to the country where the tax is lower.

It is inherent in the conception of international investment that capital should be free to flow to the places where it can earn the greatest reward consistent with the minimum risk of loss. The investor considers the reward on an investment to be only the net yield after the tax. If a country seeking capital tried to attract capital by having a low rate of tax on income it is desirable that it should be free to do so. It is wrong that the country which provides the capital should thwart the attempt of the under-developed country, by annulling the inducement of a low local tax by imposing a supplementary tax at home. That is a form of protection designed to reserve the first call on available capital to domestic enterprises. Sufficient protection is provided for them by the normal inertia or reluctance to venture capital abroad because of the greater risk. It does not need to be supplemented by an additional tax to take away the extra attraction which is provided by a low foreign tax.

(e) Local Tax Concessions

It is in this field that countries which hold out special tax concessions to private enterprise to set up new business in their country to develop it, have a definite grievance against countries which tax foreign income to the ordinary rates of tax and give a credit for the foreign tax. Whatever relief the capital-importing countries give to foreign capital which is invested in their countries merely serves to reduce the rebate which the capital-exporting countries give to their residents. Therefore the tax relief is never enjoyed by the persons who invest the capital, but is expropriated by their government. As a result, the tax concessions which are held out by capital-importing countries entirely fail in their attempt to attract capital. It is not in discussion at this point whether the capital-importing country is wise in offering such tax concessions. The point which is made is that the foreign tax credit system adopted by the capital exporting country robs the investor of the benefit.

(f) A Bar to Choice of Re-Investment

The claim by the country of residence to tax foreign income of its residents interferes with the free flow of money for investment in other territories. The profits earned in one territory may not be required there or may be more urgently required in another territory. The resident tax payer may desire to re-invest his profits in a different overseas country. If he cannot get possession of his surplus income without paying a supplementary tax in his country of residence, he will have that amount less to invest in the other overseas country and, what is probably worse, he may refrain from drawing the income and re-investing it altogether. In that event, the country needing the capital is deprived of a possible source of supply.

(g) Objections Based on Presumed Reduction in State Revenues

The governments which defend the tax-credit system against the system of exempting foreign income from home taxes, usually fall back on the last argument that the Treasury cannot afford the loss of revenue which would be caused by a change. When asked to quantify this potential loss of revenue they are in a difficulty. They can only answer that if the income had been exempted in past years, the tax actually levied on it would not have been levied. But this answer ignores the effect on that income of relieving it of tax in the country of residence ; it only measures the tax which was levied on the income which did come home. It does not consider the income which might have come home but did not come home because of the home tax. The missing flow of income includes not only profits which have been earned abroad in foreign subsidiary companies and kept there, but also potential income which was never earned because the yield after tax did not justify the venture.

A liberal fiscal policy in this regard will pay for itself in the increased flow of trade and of profits at home, which will increase the yield of the taxes on domestic profits and on personal consumption. It is clear that the free movement of capital is as important as the free movement of goods in the liberation of international trade. It is necessary to give up discouraging investments abroad. It is necessary to suppress the checks and impediments to the movement of capital between countries. The removal of double taxation, by cancelling taxes levied on foreign income in the country of residence would be an essential step in this move to freedom. In fact all countries would benefit, even the country of residence, if not at once then certainly in the future, by the rise in the volume of international trade which would certainly follow.

IV. A COMPARISON ON TECHNICAL GROUNDS

Technically, as a means of removing double taxation, the exemption procedure is superior to the tax credit procedure on the following grounds:

(a) Similar Taxes

The tax credit method can only credit income taxes against similar taxes. If the country where the income is earned obtains its revenue by other means than income or profits taxes, such as taxes on capital or on sales or services or even on an arbitrary figure which takes into account the size of the capital of the payroll, or of the turnover, no relief against double taxation is possible beyond charging the tax against the income instead of against the tax.

The exemption method completely eliminates double taxation.

(b) Bases of Assessment

Differences in bases of assessment can render the tax credit method ineffective because relief is given to the extent of the lower of the two taxes, the home tax or the foreign tax.

If the assessment is high in the foreign country and low in the home country in a given year, and the converse arises in a following year, the relief for the two years falls short of the foreign tax for the two years.

(c) Plurality of Taxes

Where the foreign income has borne more than one tax, such as a tax on the profits of a company and a tax on the dividend paid, the foreign tax credit frequently gives relief only in respect of the tax deducted from or charged on the dividend. Likewise, if the income has borne a municipal or provincial tax as well as a central government tax, relief is given only in respect of the central government tax. The same situation arises if the income passes through more than one country and suffers a tax in each, because the foreign tax credit takes account only of the last tax.

If any one tax in respect of which relief is given is equal to or greater than the home tax, the effect on the tax credit method is the same as the exemption method but in any other case the tax credit method does not give as much relief as the exemption method.

(d) Administration:

It is alleged that there will be difficulties in defining the source of income precisely if the jurisdiction of a country is limited to income arising within its borders, which difficulties will not arise in the case of residents if they are taxed on their world income. This is true, but it should be recalled that those types of difficulties exist already in the case of non-residents. All that can be said is that the number of cases where a definition is required will be greater under the exemption method than under the tax credit method.

In the other direction, all the detailed labour involved in discovering and examining the foreign tax assessment so as to calculate a foreign tax credit claim will have disappeared. Taking the two factors together there should be less administrative work.

(e) Avoidance of tax

It is also alleged that if exemption were granted for foreign income there would be an incentive to divert income from the more heavily taxed country of residence to a lighter taxed country of origin. Also the definitions of the situation of income might furnish a ready means to practise such diversion because of their vagueness.

This argument is not admitted to be a new factor. Diversion of profits is possible under any circumstances, and the trend is bound to be away from heavily taxed countries. It is in this connection that the treaties can provide a useful check on the statements made by the taxpayer in the country of residence, as to the amount and character of the income arising from operations abroad. For instance, a manufacturer selling to a subsidiary company abroad may undercharge his subsidiary, if the rate of tax is lower in the country where the subsidiary is situated. Per contra, he may overcharge it, if the rate of tax is higher. This can happen whether the country of residence adopts the exemption system or the tax credit system.

The profits which would have otherwise accrued to the seller, or to the buyer, as the case may be, are known as "diverted" profits. The standard bilateral treaties provide for exchange of information between the tax officers of the Contracting States to discover such diverted profits and to tax them as if the trade had been done with independent persons.

That machinery would be available, and would be used in cases where the exemption system was adopted, if it were accompanied by a treaty with the country of origin. Any exaggeration of the amount of the foreign income, in a statement by a taxpayer in the country of the residence for the purpose of claiming examption could be verified with the tax officers of the country of origin.

There is no insuperable difficulty in defining fairly concisely the source of different types of income. The double taxation treaties furnish workable criteria. Suggested model principles were outlined by the ICC in Brochure No. 146 in describing the requirements for legislation for unilateral relief.

V. THE FUNCTION OF BILATERAL TREATIES

If all countries agreed to limit their taxes to income arising within their jurisdiction and to exempt income arising to their residents from foreign sources, double taxation would disappear, except in cases where the definitions of sources adopted by different countries overlapped. Similarly, if the definition fell short, there would be gaps through which income would pass untaxed.

There would, therefore, be two useful purposes to be served by bilateral treaties, namely to bind a country to adhere to the model definitions of source on a basis of reciprocity, and secondly to provide for exchange of information in order to ensure that income which was by definition outside the country of origin was attributed to the country of residence so that nothing was omitted and nothing was duplicated.

VI. TAXATION OF THE NON-RESIDENT IN THE COUNTRY OF ORIGIN

If it is proposed to distinguish the income of a person who is resident in a country into two parts, namely income which arises within his own country, which should be fully taxed, and income which arises to him from foreign sources, which should be exempt in the country in which he resides, it is necessary to examine how this thought can be applied without offending other familiar tax principles.

To examine the situation of such a taxpayer as a whole it is necessary to consider first how the income should be taxed in the foreign country where it arises. The exemption system presupposes that there is no connection between the taxes levied in the country of origin and the taxes, if any, to be levied in the country of residence. The only stipulation is that the income is liable to be taxed in one or the other but not in both, and that it is allocable to one or the other in the definitions of source. If the country of origin desires for its own reasons to exempt the income allocable to it, that is no concern of the country of residence and no ground for a claim for tax by it.

The principle of territoriality pre-supposes that the country of origin should not attempt to tax the income which arises within its jurisdiction by reference to the existence or amount of any income which arises outside its jurisdiction, is that to say, it should not tax the income at a rate of tax which is dependent upon the declaration by the taxpayer of his world income. The reason for this is that it cannot control the accuracy of the declaration, either by its own resources or by asking for the aid of the taxing authority of the country of the country of residence. Since it cannot tax by reference to total income, the country of origin has the alternative of either taxing the income to a proportional tax without any graduation for domestic circumstances, or of taxing the income to the progressive tax on the assumption that the income is the total income. There is nothing in this decision which can be helped by bilateral treaties or by a condition of reciprocity, because the stipulation is that the tax in the country of origin does not concern the government of the country of residence. The decision has to be left to the country of origin in the light of its own interests. It can be fairly certain that if its tax is onerous on non-residents, it will be shunned by them. If its tax is light on non-residents, they will be attracted, other things being equal, to provide capital, goods and services.

It is accepted international practice not to impose heavier taxes on citizens of other countries than are imposed on citizens of the country concerned. Often this principle is included in general treaties of friendship or in a tax avoidance

agreement. If in pursuance of this principle the country of origin gives the option to the non-resident to pay tax on the same terms as a resident of that country, then such an arrangement would be useful relief in derogation of the general principle, which would particularly benefit pensioners and persons with small incomes.

One practice is to be deprecated which is attempted from time to time in pursuit of the non-resident. It has been claimed that because income arises in the country of origin, that country has the right to follow through and to tax that income on non-resident persons who may become successively entitled to that income. Claims have been made to tax shareholders in a non-resident company, in respect of dividends received by them from the non-resident company, by reason of the fact that the profits which provided the dividends were derived from the country of origin. Because the claim is unenforceable on the non-resident shareholder, pressure has been put on the company to pay the tax.

There is no merit of any kind in this claim. The country of origin can only look at the taxpayer who is present in its jurisdiction—in this case the limited company—and levy tax on it in relation to its profits or income. At that point its right to tax is exhausted. There can be no additional claim on persons subsequently entitled to receive the income outside the jurisdiction.

VIII. TAXATION IN THE COUNTRY OF RESIDENCE

The exemption system requires that the income from foreign sources should be exempt in the country of residence. If the country of residence has adopted a progressive tax which increases in severity as the total income arises, the exemption system conflicts with the principle of the progressive tax by no means sacred, and it can be that when other taxes are taken into account, such as taxes on wealth, on successions, on gifts and on consumption, which are present in the integrated fiscal structure of the country, a progressive tax is itself unjustified. But apart from that thought, the pure principle of progression has largely been abandoned when the progressive tax payable in the country of residence is agreed to be abated by the tax which has been paid on the income in the country of origin.

There is, however, a problem to be considered in calculating the amount of the progressive tax on the income which is derived from home sources. Assuming that the foreign income is exempt from the tax in the country of residence, it is still part of the total income of the resident taxpayer. It can be regarded as the first part of the total income, in which case any income from home sources is regarded as the higher part of the total income for the purpose of taxing the income from home sources. In the second place, the foreign income can be regarded as being spread equally with the home income in each ascending step in the total income ; in that case, the home income would be taxed at the average rate of tax which would be proper to the total income (but no tax would be levied on the foreign income).

In the third place, the foreign income can be regarded as the last part of the total income ; in that case the income from home sources would be taxed at the rates applicable to the lower part of the total income. To do this would in fact be to ignore completely the foreign income for the purpose of levying tax on the income from home sources.

It may seem on a comparison of the three choices that the middle course is a fair compromise, namely to regard the home income as being taxable at the average rate of tax which is appropriate to the total income including the foreign income. The Commission, however, expresses no preference for this course over the third course, but it would deprecate the first course as being discriminatory. The choice should be with the respective governments of the countries of residence and their choice should be guided by the motive of encouraging

investments overseas so far as is consistent with their general fiscal structure.

In the case of a company the progressive rate does not normally apply and the calculated rate would not be needed.

The situation of a shareholder receiving a dividend from a company, part of whose income has borne foreign tax and part has borne the home tax, depends upon the general system of taxation of corporate bodies in the respective countries. Some countries tax dividends in the hands of the shareholders or by deductions at source without regard to the tax paid by the company on its profits. In such cases the treatment of foreign income in the hands of company raises no new future. Other countries modify or exempt the tax payable by the shareholders by reference to the tax paid by the company on its profits.

In such cases, the modification or exemption of the tax payable by the shareholders can be continued, because the assumption remains the same, namely that the company has paid all the tax which requires to be paid on its profits, whether its foreign income is exempted or is the subject of a foreign tax credit.

VIII. CONCLUSIONS

The sum up, the Commission wishes to emphasize the following considerations in its report, namely :

(a) The claim of the country of residence to tax income derived from the country of origin rests largely on historical grounds which are out of keeping with existing conditions ; at the most the country of residence is only entitled to a proportionate share of the total tax on the income which is commensurate with the contribution it makes to the production of the income. This, in the nature of things, must be small in relation to the contribution made by the country of origin.

(b) From the economic point of view, the claim of the country of residence to tax income of foreign origin is prejudicial to the interests of the country of origin, inasmuch as it checks the development of countries which are in need of capital, by discouraging new capital from being invested there and by taking away the portion or profits which might be available for re-investment.

The claim to tax income of foreign origin is a form of protection to the home capital market of the country of residence which is contrary to the best interests of that country, because it is a bar to free choice of money available for international investment to flow to the places where it is most needed or where it can be most usefully employed ; such taxation is in fact an obstacle to greater productivity and the freeing of trade.

(c) From the technical point of view, the system of taxing foreign income and giving a credit for foreign taxes on it often fails to give adequate relief from double taxation owing to differences in the type of taxes levied in the country of residence and in the country of origin, in the bases assessment to income taxes, and owing to the existence of subordinate taxing authorities in addition to the central government.

In any case, the taxation of foreign income, even with deduction by the country of residence of taxes paid on it abroad, nullifies the advantages for private capital of moderate rates of tax in the country of origin.

For these reasons, the Commission concludes :

1. The country of origin, that is, the country from which the income is derived, has the sole right to tax the income. The problem of double taxation arises from the claim of the country of residence to tax income of foreign origin. The only sure method of avoiding double taxation is for the country of residence to exempt foreign income from any proportional or progressive tax.

2. In order to achieve this, internationally acceptable rules can be made to define the allocation of income to the

country where it is deemed to arise for the purpose of taxation. Bilateral treaties, open to adherence by others, can be made to adopt such rules on a reciprocal basis and to exchange information so as to secure that income as allocable to one country only. Alternatively any country may apply such standard rules unilaterally or in relation to income derived from another country which has also adopted them.

The rates of tax charged by the country of origin should not favour its own residents and discriminate against non-residents. In fixing the amount of the tax payable by a non-resident taxpayer, the country of origin should not take into account any income arising outside its jurisdiction, nor should its claim to tax be pressed any further than the first non-resident person who is entitled to the income, whether the tax is collected at source or by direct assessment.

Finally, the Commission recalls that even if all the double taxation were eliminated by the method outlined above, since it is the country of origin which alone decides the rate of tax to be charged on the income arising within its jurisdiction, it will ultimately depend on the taxing authorities of of that country to attract or repel capital from abroad.