COMPARATIVE INCOME TAXATION: A STRUCTURAL ANALYSIS

Principal Author

Hugh J. Ault, Boston College Law School

Contributing Authors

Brian J. Arnold, University of Western Ontario Guy Gest, University of Paris I Peter Melz, Stockholm University Minoru Nakazato, University of Tokyo Albert J. Rädler, University of Hamburg J. Mark Ramseyer, University of Chicago Law School John Tiley, University of Cambridge Richard J. Vann, University of Sydney Kees van Raad, University of Leyden

KLUWER LAW INTERNATIONAL

The Hague • London • Boston

Table of Contents

Intro	oduction	1
Part	One: General Description	
A	Australia	5
1		5
2	•	
3	· · · · · · · · · · · · · · · · · · ·	
4		
5		
6		
7	. Administrative, taxpayer and judicial style	14
	7.1 Administrative style	
*	7.2 Taxpayer style	
	7.3 Judicial style	18
8.	. General principles	19
	8. 1 Relation of tax and financial accounting	19
	8. 2 Respect for civil law form	
9.	. Anti-avoidance legislation	21
C	anada	25
1.	. History of the income tax	25
2.		
3.	. Composition of fiscal system	26
4.	. Tax rates	26
5.	. Basic structure of the system	27
6.	. Statutory style	29
7.		
8.	The role of the courts	31
9.	The Canadian self-assessment system	32
10	O. Revenue Canada's administrative style	32
11		
12	2. Relation of tax and financial accounting	34
13	3. Respect of civil or private law form	35
14	4. Substance over form	
1.5	5. Anti-avoidance doctrines and legislation	36

Frar		39
1.	History and basic structure of the tax system	. 39
	1.1 General outline	. 39
	1. 2 The individual income taxation system	
2.	Rate structure	41
	2.1 Individual income tax	. 41
	2.2 Corporate income tax	. 42
3.	Basic structure of the tax system	. 42
4.	Statutory style	. 43
5.	Statutory interpretation and judicial style	. 44
6.	Administrative style	. 45
	6.1 Administrative interpretations	. 45
	6.2 Tax audits	. 46
7.	Taxpayers' style	. 46
8.	Relation of tax and financial accounting	. 47
9.	Respect for civil law	. 47
10.	Anti-avoidance doctrines and rules	
11.	Tax assessment	. 48
Cor	rmany	40
1.	Power to enact tax laws	
2.	Sharing of tax revenue	
3.	Administrating taxes	
<i>3</i> . 4 .	Significance of taxes	
т.	4.1 Importance of individual taxes	
	4.2 Shift from direct taxes to indirect taxes	
5.	Personal income tax	
٦.	5.1 Tax base	
	5.2 Tax rates	
6.	Corporate income tax	_
7.	Trade tax on income and capital	
8.	Statutory style	
9.	Impact of the Constitution and the Federal	. 00
	Constitutional Court	61
	9.1 Basic rights	
	9.2 Important decisions	
10.		
11.	, F	
12.		
		•• ••

	12.1 Tax filing and audit enforcement	. 64
	12.2 Differences in tax compliance	
13.	Appeals against tax assessments	
14.		
	14.1 Federal Tax Court (Bundesfinanzhof)	
15.	Administrative style	67
16.	Taxpayer's style	
17.	Relation of tax and financial accounting	
18.	Respect of civil or private law	
19.	Substance over form	
Japa	an	71
1.	History	71
2.	Basic structure of the system	74
3.	Rate structure	74
4.	Composition of fiscal system	75
5.	Statutory style	
6.	Statutory interpretation	
7.	Administrative style	76
8.	Taxpayer style	
9.	Judicial role and style	
10.	General principles	
	10.1 Relation of tax to financial accounting	
	10.2 Extent of respect for civil law form	
	10.3 Anti-avoidance doctrines or legislation	
11.	Procedure	
The	Netherlands	81
1.	Tax system	81
2.	History of the Netherlands tax system,	
	tax morale and tax simplification	82
3.	Statutory and judicial style and role	83
	3.1 Statutory style	83
	3.2 Judicial role and style	
4.	Basic structure of the income tax system	
	4.1 Types of income taxes	
	4.2 Sources of income	
	4.3 Tax rates	
	A A Indevation to inflation	

5.	Statutory interpretation	88
	5. 1 In general	88
	5. 2 Respect under tax law for the civil (private)	
	law form of contracts	89
	5. 3 Substance over form	89
6.	Tax administration	
	6.1 Organization of the Revenue Service	
	6.2 Taxpayer bill of rights; ombudsman	
	6.3 Release of Government information to taxpayers	92
	6.4 Advance rulings	
7.	Tax procedure	
• •	7.1 Assessment, administrative appeal	
	and appeal to courts	93
	7.2 Impact of human rights conventions and EC Treaty	
	fundamental freedom provisions	94
8.	International	
0.	8.1 Historically-based foreign orientation	
	8.2 Double taxation relief	
	8.3 Classical system	
Sw	eden	. 97
1.	Historical development	
2.	Basic structure	
3.	Composition of fiscal system	
4.	Statutory style	
5.	Statutory interpretation	
6.	Administrative style	
7.	Taxpayer style	
8.	Judicial style	
9.	General principles	
٠.	9.1 Relation of tax and financial accounting	
	9.2 Respect of civil law	
	9.3 Anti-avoidance	
10.		106
10.	r rocedure	100
Ur	nited Kingdom	100
1.	The principle direct taxes	
1.	1.1 Income Tax	
	1.2 Capital Gains Tax (CGT)	109
	1.3 Corporation Tax	114
	1.5 Corporation lax	114

	2.	Indirect taxes	113
	3.	Constitutional structure	110
	4.	Rate of tax	117
		4.1 History and politics	117
		4.2 Inflation	
		4.3 Rate structure and reliefs, 1996	117
	5.	Tax setting	
		5.1 Administration	
		5.2 Avoidance of tax	121
		5.3 Sources of law, official practice and rulings	
	6.	Role of courts	126
		6.1 Judicial review	126
		6.2 Appeal system	127
	7.	The current situation	128
	Un	ited States	131
	1.	History of the federal income tax	131
	2.	Constitutional issues	132
	3.	Tax rates	133
	4.	Composition of fiscal system	135
	5.	Basic structure of income tax for individuals	137
	6.	Basic structure of the corporate income tax	
	7.	Statutory style	144
	8.	Statutory interpretation	145
	9.	Administrative, taxpayer and judicial style	147
		9.1 Administrative style	147
		9.2 Taxpayer style	148
		9.3 Judicial structure and style	149
	10.	Relationship of tax and financial accounting	149
	11.	Anti-avoidance legislation	150
	12.	Future developments	151
Paı	rt Tv	vo: Basic Income Taxation	
	Sub	part A: Inclusions in the tax base	155
	1.	Employee fringe benefits	157
		1.1 General	157
		1.2 Employer-provided pension benefits	165
	2.	Imputed income from owner-occupied housing	172

3.	Gifts	75
•	3.1 Gifts outside of a business context ("personal" gifts)	176
	3.2 Gifts in a business or employment context	
4.	Prizes and awards	
5.	Scholarships and grants	
6.	Cancellation of indebtedness	
7.	Gambling	
8.	Illegal income	
9.	Windfalls	
10.	Subsidies	
11.	Realization and recognition of gain	
12.	Capital gains and losses	194
	Cupital game and locate	
Sul	ppart B: Deductions	204
1.	Mixed business and personal expenses	
••	1.1 Commuting	
	1.2 Moving expenses	
	1.3 Clothing	
	1.4 Business travel	
	1.5 Business entertainment	
	1.6 Child care	
2.	"Hobby losses" and the criteria for determining	
	business versus personal activities	222
3.	Capital costs and recovery methods	
	3.1 Determining capital costs	
	3.2 Capital cost recovery systems	
4.	Educational costs	
5.	Deduction of personal costs	
٥.	5.1 Interest	
	5.2 Personal losses	
	5.3 Medical expenses	
	5.4 Charitable deduction	230
6.	Limitations on deductions and losses	233
٠.	6.1 Illegal payments, fines and penalties	241
	6.2 Expense associated with tax-exempt income	243
	6.3 "Quarantining" and other limits or	47 3
	restrictions on certain categories of expenses	245
		475

	Sul	ppart C: Accounting	. 250
	1.	Basic accounting methods	250
	2.	Inclusion of advance payments	
	3.	Income treatment of deferred payments	
	4.	Original issue discount obligations and other	
		complex financial instruments	260
	Sub	ppart D: Attribution of income	. 269
	1.	Definition of taxable unit	270
	2.	Alimony and child support	276
	3.	Limitations on assignment of income	280
Par	t Th	ree: Taxation of Business Organizations	
	Sub	part A: Corporate-Shareholder Taxation	. 285
	1.	Overview of corporate tax systems	
	2.	Defining entities subject to tax	
	3.	Issues in corporate formation	
	4.	Issues involving capital structure	
	5.	Taxation of corporate distributions	
		5.1 Basic structure of distribution rules	302
		5.2 Relating distributions to corporate earnings	304
		5.3 Constructive dividends	
		5.4 Intercorporate dividends	308
		5.5 Distributions of appreciated or depreciated property	311
		5.6 Distributions involving changes	
		in corporate structure	313
		5.6.1 General	
		5.6.2 Stock dividends	314
		5.6.3 Redemptions	317
	6.	Liquidations	320
	7.	Corporate reorganizations and restructuring	324
		7.1 General	324
		7.2 Merger transactions	325
		7.3 Share exchanges	
		7.4 Nonmerger asset reorganizations	333
		7.5 Corporate divisions: "Demergers"	
	8.	Transfer and limitations on transfer	
		of corporate tax attributes	340

	9.	Consolidated corporate taxation	343
	10.		348
	10.	oponii un roganii i	
	Sub	part B: Partnership Taxation	354
	1.	Qualification for pass-thru taxation	355
	2.	Basic structure of pass-thru taxation	356
	3.	Liabilities, basis and losses	360
	4.	Transactions between partner and partnership	
	5.	Disposition of partnership interest	
	6.	Liquidation of the partnership	365
Par	rt Fo	ur: International Taxation	
	Sub	ppart A: Residence Taxation	368
	1.		
		1.1 Individuals	368
		1.2 Corporations	371
	2.	Change of status	373
		2.1 Change of status of individuals	373
		2.2 Change of status of corporations	376
		2.3 Dual residence	379
	3.	Mechanisms for relief of double taxation	380
		3.1 Issues in the structure of a foreign tax	
		credit system	385
		3.1.1 Creditable taxes	385
		3.1.2 Limitations on the credit	388
		3.1.3 Allocation of expenses to foreign-source income	391
		3.1.4 Treatment of losses in the credit computation	
		3.1.5 Carryover of excess credits or limitation	396
		3.1.6 Indirect credit for foreign taxes paid by	
		foreign subsidiaries	
		3.1.6.1 Share ownership requirements	398
		3.1.6.2 Tier Limitations	399
		3.1.6.3 Computation of the indirect credit	399
		3.1.7 Interaction between indirect credit	
		and limitation system	400
		3.2 Issues in the structure of an exemption	
		for foreign income	402

	3.2.1 Structure of the exemption
	3.2.2 Classes of exempt income
	3.2.3 Allocation of deductions to tax-exempt income 400
	3.2.4 Treatment of foreign losses
4.	Limitations on exemptions or deferral of income
	of foreign corporations409
	4.1 Limitations on exemption for shareholders in
	foreign corporations with significant domestic
	share ownership411
	4.2 Limitations on deferral for shareholders of foreign
	corporations with significant domestic
	share ownership
	4.3 Special provisions dealing with domestic portfolio
	investment in foreign investment companies422
5.	Outbound transfers to foreign branches or subsidiaries425
	-
Su	bpart B: Source Taxation431
1.	Issues in the structure of net basis taxation
	of business income431
	1.1 Threshold of activity431
	1.2 Attribution of business income for net basis taxation434
	1.3 Determination of deductions in the net basis
	taxation of business income439
	1.4 Taxation of employment income442
	1.5 Other situations involving net basis taxation444
2.	Issues in the structure of gross basis taxation445
3.	Branch profits tax
4.	Limitations on base-eroding payments to nonresidents452
5.	Restrictions on source-based taxation of nonresidents
	within the European Union455
	, , , , , , , , , , , , , , , , , , ,
	ppart C: Additional International Topics
l.	Special international anti-avoidance rules
2.	Selected intercompany pricing issues
3.	Selected treaty issues
	3.1 Relation between domestic law and treaties;
	treaty override
	3.2 Approach to treaty interpretation469

KVIII COMPARATIVE INCOME TAXATION: A STRUCTURAL ANALYSIS

3.3 Anti-treaty shopping policy	471
3.4 Nondiscrimination	
3.5 "Model" treaties	476
3.6 Tax sparing by treaty	478
Part Five: Selected Bibliography	481
Index	533