

Tax Reform

— — Bizonal Income Levies Adjusted

THE BIZONAL Economic Council Ordinance No. 95, "(Second) Ordinance on the Provisional Revision of Tax Legislation," was approved by the Bipartite Board after assurance from the German authorities that they did not contemplate further tax revisions before the formation of a western German government. The background of the ordinance antedates monetary reform of June 20, 1948.

The German Bizonal Economic Council had made proposals in May 1948 for considerable reductions in the principal taxes, the most important relating to the income tax, in regard to which the German authorities wished to make an all-round reduction in rates at that time. Military Government considered, however, that the proposed reductions might be too sweeping. On all sides the desirability of uniformity of taxation throughout the three western zones was recognized.

Finally a compromise in rate reduction, which also achieved uniformity, resulted in US and British Military Government Law No. 64, "Provisional Revision of Tax Legislation," of June 20, 1948. Similar laws were passed by the states of the French Zone. This law brought into force new tax tables which, although they represented a considerable relief, did not go so far as the German authorities had wished.

AS SOON as the transition period immediately following monetary reform had ended, the German authorities again pressed for further income tax reductions. Two main arguments were advanced by them. The first was that the rate of tax on the middle and higher income groups was still so great that it encouraged tax evasion.

It was argued that if a businessman declared and paid a tax on his actual profits, the amount remaining to him would not be sufficient to provide for maintenance and at the same time to finance replacements of business assets which had been lost as a result of the war or which had become unserviceable in the normal course of business.

Moreover, it was emphasized as a second point that the success of the European Recovery Program (ERP)

Excerpt
from **Monthly Report, No. 46**
of the US Military Governor

in the Bizonal Area made it essential that capital for medium- and long-term investment in reconstruction be made available by appropriate taxation concessions.

The German Bizonal Department for Finance, therefore, set out to prepare an ordinance which would provide sufficient tax relief to improve the standard of tax-honesty and would probably stimulate saving. The first draft of this ordinance, which was submitted in November 1948, provided for an all-round reduction in tax rates to the levels which had been proposed, but only partially approved, in May 1948, and for a form of tax amnesty for tax offenses committed before, and at the time of, monetary reform.

As these proposals were not acceptable to Military Government or to certain German elements, a series of re-drafts was made, in the course of which the amnesty proposals and those for a general reduction in tax rates were abandoned. The ordinance which was finally passed by the Economic Council in March 1949 bore little resemblance to the original draft. It consisted of a series of specific income tax concessions which, in many cases, are extensions of the concessions given in MG Law No. 64.

THE PRESURRENDER German law contains a provision for writing off of normal depreciation in the annual balance sheets of businesses. Law No. 64 introduced for the first time the principle of provision for the writing off of a special initial allowance with respect to replacements of business assets made after Dec. 31, 1948, a concession modeled on certain provisions of the British Finance Act of 1945.

This principle was extended by Economic Council Ordinance No. 95, which permits allowances to be granted with respect to such business assets as plant equipment (a maximum of 50 percent in the first two years), dwelling houses (10 percent in each of the first two years), ships (15 per-

cent in each of the first two years), and factory and farm buildings (10 percent in each of the first two years). Furthermore, grants or non-interest-bearing loans made to various public and private housing organizations are to be allowed as a deduction in arriving at the profit which is subject to tax.

Law No. 64 extended the allowances granted for such categories of expenditure as small savings; contributions to charitable, religious and scientific organizations; payments to insurance and building societies; and investments in cooperative societies and other approved concerns.

The increased limits of such "special expenditure" were DM 600 (\$180 for a single man and DM 900 (\$270) for a married man, with further increases for each dependent child. If the expenditure under the headings named exceeded these limits, three-eighths of the excess was allowed, subject to a ceiling of 15 percent of the taxpayer's income or DM 20,000 (\$6,000), whichever was less.

Ordinance No. 95 extends all these limits. In the case of a single man, complete relief is given on DM 800 (\$240) instead of DM 600; in the case of a married man, on DM 1,200 (\$360) instead of DM 900, and so on. On expenditure in excess of these limits the proportion to be exempted is increased from three-eighths to one-half, and the ceiling from DM 20,000 to DM 30,000 (\$9,000). Furthermore, in the case of taxpayers 50 years of age and upward, their time for saving being limited, these limits are doubled.

ANOTHER existing tax provision gave relief to the extent of 50 percent of the retained profits of a business, subject to the proviso that the retained portion concerned must not exceed 10 percent of the aggregate profits. Ordinance No. 95 raised this ceiling to 15 percent.

One of the anomalies in the old German income tax law, as amended by Law No. 64, was that the aggregate amount of income and property taxes might—in the case of very wealthy taxpayers—exceed 100 percent of their incomes. By making property tax a

(Continued on next page)

deduction in computing income tax assessments, Ordinance No. 95 removes this anomaly.

The most novel provision in Ordinance No. 95 is that by which special relief from the application of the higher tax brackets is given, provided that profits are not spent. This provision was prompted largely by the disparity of the treatment formerly accorded to the owner of an incorporated business, as compared with that given the "one man" G.m.b.H. (private company).

Whereas companies (corporations) are taxed at the uniform rate of 50 percent, the owner of an unincorporated business was charged on a progressive scale which, in the case of an income of about DM 30,000 (\$9,000) gives an average rate of about 50 percent. Any surplus above this limit was, however, taxed at rates ranging from 78 to 95 percent.

Ordinance No. 95 gives a taxpayer who owns a business the option of paying at 50 percent only on his total income, provided that he complies with two conditions: (1) he must restrict his drawings for personal consumption to DM 15,000 (\$4,500) this being DM 30,000 less the tax; and (2) he must earmark the balance of retained profits and either use it in his own business or invest it in long-term securities such as those of the Reconstruction Loan Corporation.

IN VIEW of the fact that this provision might have led to the plowing back of business profits into economically undesirable enterprises (for example, night clubs at the present time), it is stipulated that the earmarked profit which a taxpayer may reinvest in his own business is to be limited to that proportion which is represented by the value of the business assets divided by the turnover. This ingenious device weights the balance in favor of productive concerns generally and heavy industry in particular where the greatest need for replacement exists.

To illustrate the working of this provision, the following example is given of the case of a private business earning an annual profit of DM 80,000 (\$24,000):

	Law No. 64	Ord. No. 95
Total Profit	DM 80,000	DM 80,000
Tax Payable	57,600	40,000
Net Balance	22,400	40,000
Compulsorily Retained	Nil	25,000
Maximum Personal Drawings	22,400	15,000

A minor relief, which also has as its origin an attempt to alleviate the steepness of the progressive scale, consists in a concession to professional men and employees who derive a subsidiary income from some scientific, literary or artistic source, as, for example, lecture fees. They are to be charged on this income at a special rate, which may vary from 10 to 40 percent according to circumstances.

THE SAME motive—the desire to minimize the deterrent effect of the progressive scale—has led to the almost complete exemption from taxation of overtime pay. Where more than normal hours are worked the extra pay has two elements—the additional pay on a normal time basis, and the further addition in pay derived from higher time rates. Ordinance No. 95 provides that the first of these elements shall be taxed at five percent only, and that the second shall be tax free. Furthermore, Sunday, holiday and night work are completely exempted from tax. Thus wage and salary earners are given a substantial tax relief.

Most of the other reliefs operate in favor of the businessman, as it is

from him that the greatest contribution toward new capital formation is to be expected. Law No. 64 contained a provision granting religious, and scientific institutions. The limits of this relief insofar as donations to charitable and scientific organizations are concerned are very slightly extended by Ordinance No. 95.

THE ORIGINAL plan of the Bizonal Department for Finance was to link up an offer of an amnesty on the one hand with the threat of more stringent penal provisions on the other. The amnesty proposals have been abandoned, but the application of a more stringent penal procedure is provided for.

The definition of what constitutes "voluntary disclosure" is slightly extended in the taxpayer's favor. Where a taxpayer was guilty of irregularities in connection with the special inventory taken at the time of monetary reform, he may compound for penalties against tax laws and economic regulations by making a "repentance payment" of 10 percent of the underpaid taxes. There is a slight increase in the rate of interest charged on arrears. + END

Belgian Diamond Claim Clarified

US Military Government officials, commenting on the allegations made by the Federation of Belgian Diamond Exchanges that Military Government had refused to reconstitute enormous quantities of polished and industrial diamonds to Belgium, pointed out that the statement made by the Federation that the Belgian authorities had established beyond doubt its right to practically the whole of those properties is a misrepresentation of the facts.

The Belgians failed to establish identification which is required for the restitution of such properties, said Mr. Orren R. McJunkins, chief of the Reparations and Restitution Branch, Property Division, OMGUS. Mr. McJunkins asserted:

"In an attempt to obtain these properties the Belgian representatives insisted that Military Government permit Belgian-designated experts to inspect these properties, but this request was denied for obvious reasons. Military Government engaged an independent group of experts to determine whether or not the dia-

monds could be identified and its findings were that identification was impossible.

"As a result of this determination, no further consideration could be given to the Belgian claim for the diamonds. Had the Belgians been able to identify these diamonds it would have still been necessary for them to establish the fact that these diamonds were physically in Belgium at the beginning of the German occupation of that country."

As to the 50,000 carats of polished diamonds alleged by the Belgians to have been seized by the Germans, MG officials state that they have no knowledge of the whereabouts of these properties and so far have not been provided with any information that might lead to their recovery.

Military Government has worked out a plan for disposal of the industrial diamonds by sale for use in the German economy in small lots to prevent flooding the market, and at such prices as are established for current imports. Sale of those properties has already started.