APPENDICES
### APPENDIX A

#### NET FLOW OF CAPITAL TO DEVELOPING COUNTRIES (MILLION US DOLLARS)

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Official Capital</th>
<th>Private Capital</th>
<th>Percentage of private in total Col. 4 on Col. 2</th>
<th>Components of Private Capital (with percentages in brackets)</th>
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Sources:

## APPENDIX B

### NET FLOW OF CAPITAL TO SOUTH ASIA (INDIA, PAKISTAN, SRI LANKA, BANGLADESH, NEPAL, BURMA) (MILLION US DOLLARS)

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<th>Direct</th>
<th>Percentage share of South Asia in Total Flow to Developing Countries</th>
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**Sources:**
## APPENDIX C

### OUTSTANDING EXTERNAL PUBLIC DEBT OF DEVELOPMENT COUNTRIES (INCLUDING UNDISBURSED) (MILLION US DOLLARS)

**A. All Developing Countries**

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<tr>
<th>Year ending</th>
<th>Total</th>
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<th>Private</th>
<th>Suppliers and Financial Institutions (percentages in brackets) in Private</th>
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**B. South Asia**

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**Note:** The difference of Col. 4 andCols. 6 and 7 is made up of other private debt.

**Source:** World Bank, Annual Report, 1982
## FOREIGN PRIVATE CAPITAL IN INDIA (MILLION RUPEES)

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<td>1,122</td>
<td>1,130</td>
<td>1,338</td>
<td>1,278</td>
<td>1,277</td>
<td>1,262</td>
<td>1,252</td>
<td>1,259</td>
<td>1,199</td>
</tr>
<tr>
<td>Mining</td>
<td>115</td>
<td>93</td>
<td>124</td>
<td>114</td>
<td>94</td>
<td>97</td>
<td>108</td>
<td>100</td>
<td>109</td>
<td>135</td>
<td>159</td>
<td>154</td>
<td>151</td>
</tr>
<tr>
<td>Petroleum</td>
<td>223</td>
<td>1,040</td>
<td>1,486</td>
<td>1,830</td>
<td>1,709</td>
<td>1,607</td>
<td>1,921</td>
<td>1,964</td>
<td>1,957</td>
<td>1,866</td>
<td>1,749</td>
<td>1,757</td>
<td>1,716</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>707</td>
<td>1,271</td>
<td>2,201</td>
<td>4,516</td>
<td>5,133</td>
<td>6,076</td>
<td>6,917</td>
<td>7,937</td>
<td>8,725</td>
<td>9,308</td>
<td>9,513</td>
<td>9,885</td>
<td>10,500</td>
</tr>
<tr>
<td>Services</td>
<td>1,079</td>
<td>1,128</td>
<td>970</td>
<td>1,739</td>
<td>1,933</td>
<td>2,720</td>
<td>3,367</td>
<td>3,262</td>
<td>3,247</td>
<td>3,026</td>
<td>3,297</td>
<td>3,571</td>
<td>3,896</td>
</tr>
<tr>
<td><strong>Notes-continued</strong></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Contd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
NOTES:  
(a) As on 31st March of the year mentioned except for 1948 figures which are as on 30th June, 1948.

(b) The two columns for 1967 represent figures excluding and including the effect of devaluation of the rupee in June 1966.

(c) Investments in the corporate industrial and commercial enterprises, excluding insurance and banking companies and excluding also and investments from international institutions.

(d) Excludes valuation changes which together with the exclusion from total investment of investments from international institutions account for these figures being not exactly equal to the year to year changes in total investments.

(e) Direct investment includes investment in branches of foreign companies and only controlling equity investment, i.e., equity investment in Indian subsidiaries and in controlled Indian companies.

A controlled Indian company means a company with 40% or more equity capital held abroad in any one country or a company with 25% or more equity capital held by a foreign company or its nominee.

(f) Portfolio investment includes non-controlling equity investment in Indian companies and creditor capital.

(COMPiled from:

(i) Reserve Bank of India, Survey of India's Foreign Liabilities and Assets (1955).

(ii) Reserve Bank of India, India's Foreign Liabilities and Assets, 1961: Survey Report.

## APPENDIX E

### NET FLOW OF FOREIGN PRIVATE CAPITAL TO PAKISTAN (MILLION RUPEES)

<table>
<thead>
<tr>
<th>Year</th>
<th>Direct Investment</th>
<th>Supplier and Portfolio</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1957</td>
<td>79</td>
<td>118</td>
<td>197</td>
</tr>
<tr>
<td>1958</td>
<td>48</td>
<td>20</td>
<td>68</td>
</tr>
<tr>
<td>1959</td>
<td>41</td>
<td>171</td>
<td>212</td>
</tr>
<tr>
<td>1960</td>
<td>56</td>
<td>147</td>
<td>203</td>
</tr>
<tr>
<td>1961</td>
<td>67</td>
<td>24</td>
<td>91</td>
</tr>
<tr>
<td>1962</td>
<td>41</td>
<td>26</td>
<td>67</td>
</tr>
<tr>
<td>1963</td>
<td>47</td>
<td>42</td>
<td>89</td>
</tr>
<tr>
<td>1964</td>
<td>62</td>
<td>72</td>
<td>134</td>
</tr>
<tr>
<td>1965</td>
<td>37</td>
<td>50</td>
<td>87</td>
</tr>
<tr>
<td>1966</td>
<td>30</td>
<td>22</td>
<td>52</td>
</tr>
<tr>
<td>1967</td>
<td>24</td>
<td>45</td>
<td>69</td>
</tr>
<tr>
<td>1968</td>
<td>39</td>
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<td>90</td>
</tr>
<tr>
<td>1969 (n.a.)</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>1970</td>
<td>17</td>
<td>93</td>
<td>110</td>
</tr>
<tr>
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<td>40</td>
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</tr>
<tr>
<td>1972</td>
<td>-14</td>
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<tr>
<td>1973</td>
<td>-3</td>
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</tr>
<tr>
<td>1974</td>
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<td>1975</td>
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<tr>
<td>1977</td>
<td>158</td>
<td>654</td>
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<td>1978</td>
<td>267</td>
<td>575</td>
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<td>1979</td>
<td>614</td>
<td>257</td>
<td>871</td>
</tr>
<tr>
<td>1980</td>
<td>564</td>
<td>1060</td>
<td>1624</td>
</tr>
</tbody>
</table>

**Note:** Totals for 1958 and 1961 to 1968 are exclusive of portfolio.

**Sources:**

1. State Bank of Pakistan, *Foreign Liabilities and Assets and Foreign Investments in Pakistan, (1957-60).*
## Net Flow of Foreign Private Capital to Sri Lanka (Million Rupees)

<table>
<thead>
<tr>
<th>Year</th>
<th>Direct Investment</th>
<th>Suppliers and Portfolio</th>
<th>Total</th>
<th>Income</th>
</tr>
</thead>
<tbody>
<tr>
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<td>55</td>
</tr>
<tr>
<td>1951</td>
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<td>46</td>
</tr>
<tr>
<td>1953</td>
<td>-7</td>
<td>31</td>
<td>-38</td>
<td>38</td>
</tr>
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<td>-36</td>
<td>-49</td>
<td>47</td>
</tr>
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<td>53</td>
</tr>
<tr>
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<td>8</td>
<td>-4</td>
<td>41</td>
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<tr>
<td>1959</td>
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<td>-4</td>
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<td>-8</td>
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<td>44</td>
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<tr>
<td>1961</td>
<td>-6</td>
<td>12</td>
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<tr>
<td>1962</td>
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<td>3</td>
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</tr>
<tr>
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<td>4</td>
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<td>53</td>
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<td>-18</td>
<td>52</td>
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<td>-9</td>
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<td>1970</td>
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<td>-4</td>
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</tr>
<tr>
<td>1971</td>
<td>+2</td>
<td>-23</td>
<td>21</td>
<td>121</td>
</tr>
<tr>
<td>1972</td>
<td>+2</td>
<td>-39</td>
<td>-37</td>
<td>115</td>
</tr>
<tr>
<td>1973</td>
<td>+3</td>
<td>-13</td>
<td>-10</td>
<td>111</td>
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<td>1974</td>
<td>+9</td>
<td>-16</td>
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<td>-31</td>
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<td>129</td>
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<tr>
<td>1976</td>
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<td>170</td>
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<td>n.a.</td>
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<tr>
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<td>732</td>
<td>142</td>
<td>874</td>
<td>290</td>
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<tr>
<td>1980</td>
<td>710</td>
<td>3271</td>
<td>3981</td>
<td>432</td>
</tr>
<tr>
<td>1981</td>
<td>967</td>
<td>1575</td>
<td>2542</td>
<td>1675</td>
</tr>
</tbody>
</table>

APPENDIX G

CLASSIFICATION OF INDUSTRIES IN INDIA
(Industrial Policy Resolution, 1956)

Schedule A

1. Arms and ammunition and allied items of defence equipment
2. Atomic energy
3. Iron and steel
4. Heavy castings and forgings of iron and steel
5. Heavy plant and machinery required for iron and steel production, for mining, for machine tool manufacture and for such other basic industries as may be specified by the Central Government.
6. Heavy electrical plant including large hydraulic and steam turbines
7. Coal and lignite
8. Mineral oils
9. Mining of iron ore, manganese ore, chrome ore, gypsum, sulphur, gold and diamond
10. Mining and processing copper, lead, zinc, tin, molybdenum and wolfram
12. Aircraft
13. Air transport
14. Railway transport
15. Shipbuilding
16. Telephones and telephone cables, telegraph and wireless apparatus (excluding radio receiving sets)
17. Generation and distribution of electricity.
Schedule B

1. All other minerals except "minor minerals" as defined in Section 3 of the Minerals Concession Rules 1949
2. Aluminium and other non-ferrous metals not included in Schedule A
3. Machine tools
4. Ferro-alloys and tool steels
5. Basic and intermediate products required by chemical industries such as the manufacture of drugs, dye-stuffs and plastics
6. Antibiotics and other essential drugs
7. Fertilizers
8. Synthetic rubber
9. Carbonisation of coal
10. Chemical pulp
11. Road transport
12. Sea transport.
APPENDIX II

INDUSTRIES OPEN TO FOREIGN ENTERPRISES IN INDIA
(Press Note of 21 April 1982)

1. METALLURGICAL INDUSTRIES
   1. Ferro alloys
   2. Automotive castings, SG iron castings, steel castings and steel forgings
   3. Non-ferrous metals and their alloys, including aluminium foils
   4. Sponge Iron and Pelletisation

2. BOILERS AND STEAM GENERATING PLANTS

3. PRIME MOVERS (OTHER THAN ELECTRICAL GENERATORS)
   1. Industrial turbines
   2. Internal combustion engines
   3. Alternate energy systems like solar, wind, etc., & equipment therefor
   4. Gas/hydro/steam turbines from 20 MW to 60 MW

4. ELECTRICAL EQUIPMENT
   1. Equipment for transmission and distribution of electricity including power and distribution transformers, power relays, HT-switch gear, synchronous condensers
   2. Electrical motors
   3. Electrical furnaces including industrial furnaces
   4. X-ray equipment
   5. Electronic components and equipment
   6. Component wires for manufacture of lead-in-wires
   7. Hydro/steam/gas generators from 20 MW to 60 MW

5. TRANSPORTATION
   1. Mechanised sailing vessels upto 10,000 DWT including fishing trawlers
   2. Ship ancillaries

Contd...
3. (1) Commercial vehicles, public transport vehicles including automotive commercial three-wheeler jeep type vehicles, industrial locomotives

(2) Personal transport vehicles
   (i) passenger cars
   (ii) automotive two-wheelers and three-wheelers Regarding two-wheelers, only expansion of existing units, subject to an export obligation of 25% on additional capacity

(3) Specialised automotive components, such as pistons and piston rings, fuel injection equipment; auto-electricals, such as starter motors, generators, spark plugs, rear axle assembly, brake and clutch assembly, tyre/tube valves, wheels for automobiles and bimetal bearings

6. **INDUSTRIAL MACHINERY**
   Industrial machinery including specialised equipment
   1. High performance and high fidelity industrial valves as may be specified by the Ministry of Industry
   2. Centralised lubrication systems
   3. Gears, gear boxes and couplings
   4. Rolls for paper mills, rolls for rolling mills
   5. Pollution control equipment
   6. Process equipment for utilisation of recycling of wastes

7. 1. Machine tools, including controls and accessories
    2. Jigs, fixtures, tools and dies of specialised types and cross land tooling
    3. Engineering production aids such as cutting and forming tools, patterns and dies and mining tools

8. **AGRICULTURAL MACHINERY**
   Tractors

9. **EARTH MOVING MACHINERY**
   Earth Moving machinery and construction machinery and components thereof
10. **INDUSTRIAL INSTRUMENTS**
   Indicating, recording and regulating devices for pressure, temperature, rate of flow, weights, levels and the like

11. **SCIENTIFIC AND ELECTROMEDICAL INSTRUMENTS AND LABORATORY EQUIPMENT**

12. **NITROGENOUS & PHOSPHATIC FERTILIZERS** falling under
   (1) Inorganic fertilizers under '18. Fertilizers' in the First Schedule to the I (D&I) Act, 1951

13. **CHEMICALS** (other than fertilizers)
   1. Heavy organic chemicals including petro-chemicals
   2. Heavy inorganic chemicals
   3. Organic fine chemicals
   4. Synthetic rubber resins and plastic
   5. Man-made fibres
   6. Synthetic rubber
   7. Industrial explosives
   8. Technical grade insecticides, fungicides, weedicides and the like
   9. Synthetic detergents
   10. Miscellaneous chemicals (for industrial use only) including
       1. Catalysts and catalyst supports
       2. Photographic chemicals
       3. Rubber chemicals
       4. Polyols
       5. Isocyanates, Urethanes, etc.
       6. Speciality chemicals for enhanced oil recovery
       7. Heating fluids
       8. Coal tar distillation and products therefrom
       9. Tonnage plants for the manufacture of industrial gasses
       10. High altitude breathing oxygen/medical oxygen
       11. Nitrous oxide
       12. Refrigerant gases like liquid nitrogen, carbon dioxide etc. in large volumes
       13. Argon and other rare gases
       14. Alkali/acid resisting cement compound

   Contd.
14. DRUGS AND PHARMACEUTICALS

For FEDA drug companies
(a) Drug intermediates from the basic stage for production of high technology bulk drugs
(b) High technology bulk drugs from basic stages and formulations based thereon with an overall ratio of bulk drug consumption (from own manufacture) to formulations from all sources of 1 : 5

For Non-FEDA MNTP companies
All bulk drugs and formulations with an overall ratio of 1 : 10 between the value of production of bulk drugs and formulations

15. 1. Paper and pulp including paper products
2. Industrial laminates

16. 1. Automobile tyres and tubes, including automobile tyre tube valves
2. Rubberised heavy duty industrial beltings of all types
3. Rubberised conveyor beltings
4. Rubber reinforced and lined fire fighting hose pipes

17. PLATE GLASS
1. Float glass
2. Toughened glass insulators
3. Glass fibres of all types

18. CERAMICS
1. Refractories
2. Furnace lining bricks—acidic, basic and neutral
3. Ceramic fibres

19. CEMENT PRODUCTS
1. Portland cement
2. Gypsum boards, wall boards and the like

—Contd.
20. HIGH TECHNOLOGY REPRODUCTION AND MULTIPLICATION EQUIPMENT

21. CARBON AND CARBON PRODUCTS
   1. Graphite electrodes and anodes
   2. Impervious graphite blocks and sheets

22. PRETENSIONED HIGH PRESSURE RCC PIPES

23. RUBBER MACHINERY

24. PRINTING MACHINERY
   1. Web-fed high speed offset rotary printing machines having output of 30,000 or more impressions per hour
   2. Photo composing/type setting machines
   3. Multi-colour sheet-fed offset printing machines of sizes 18" x 25" and above
   4. High speed hotogravure printing machines having output of 30,000 or more impressions per hour.

NOTE:

Items of manufacture reserved for Public Sector under Schedule A to the Industrial Policy Resolution, 1956 or for production in the Small Scale Sector, as may be notified from time to time, will be excluded from the application of the list.
SUMMARY OF TAX LAWS OF INDIA, PAKISTAN, SRI LANKA AND BANGLADESH

INDIA

Income Tax

A. General: Income-tax, on corporate as well as non-corporate entities, is levied in India under the Income-tax Act, 1961, and the Income-tax Rules, 1962 framed thereunder. In respect of incomes derived from prospecting for or extraction or production of mineral oils or the provision of any services (including personal services) or facilities, ships, aircraft machinery or plant in connection therewith, the Act applies also to areas within the Exclusive Economic Zone of India extending into the sea up to 200 nautical miles from the baselines of the Indian coast. The Act

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1 Agricultural income is exempt from tax under this Act though it is added to the other income of the tax-payer for determining the rate of tax applicable to the other income. In the case of tea companies deriving composite income from the sale of tea grown as well as manufactured by them, 40% of such income is considered as non-agricultural business income in terms of Rule 8 of the Income Tax Rules.

2 Government of India, Ministry of Finance, Notification No. GSR 304 (E) of 31 March 1983 issued under Section 7 of the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones, Act, 1976.
is administered by the Central Board of Direct Taxes, a statutory body set up under the Central Boards of Revenue Act, 1963, within the Ministry of Finance of the Government of India.

The tax is charged in each assessment year, i.e., a year commencing on 1 April, at the rates prescribed in the Finance Act for that year in respect of the income of the previous year i.e., the accounting year of the tax-payer preceding the assessment year. The Act give an inclusive definition of income\(^3\) which, inter alia, includes capital gains.\(^4\)

\(^3\)Section 2 (24) of the Income-tax Act, 1961.

\(^4\)A capital gain arises on the transfer of a capital asset and represents the excess of the full value of the consideration for the transfer over the cost of acquisition together with the cost of improvement, if any, and the expenditure incurred in connection with the transfer.

'Capital asset' for this purpose means property of every kind but excludes, (a) stock-in trade, consumable stores or raw materials held for the purposes of a business or profession; (b) personal effects other than jewellery; (c) agricultural land situated in India other than land in urban areas and (d) certain gold bonds and special bearer bonds issued by the Government of India.

'Transfer of a capital asset' includes the sale, exchange or relinquishment of the asset or the extinguishment of any rights therein or the compulsory acquisition thereof under any law. (Sections 2 (14), 2 (47), 45 and 48 ibid).
The taxpayer is under an obligation\textsuperscript{5} to file a return of his total income with the jurisdictional Income-Tax Officer by 30 June of the assessment year and the Income Tax Officer has to complete the assessment and determine the tax payable within 2 years from the end of the assessment year.\textsuperscript{6} For certain specified incomes, like salaries, interest, dividends, lottery and horse-race winnings, insurance commission, payments under works contracts and payments to non-residents, tax is required to be withheld at source and paid to Government by persons disbursing such incomes.\textsuperscript{7} Balance of tax is payable in advance\textsuperscript{8} on an estimated basis in three equal instalments during the year preceding the assessment year. Any tax still payable on the returned income is required to be paid before filing the return of income.\textsuperscript{9} On completion of assessment by the Income Tax Officer, if any further tax is found payable, it has to be paid within 35 days of the service on the taxpayer of a notice of demand.\textsuperscript{10}

\textbf{B. Company:} A company is a taxable 'person' under the Act\textsuperscript{11} and pays tax levied on it in discharge of its own

\begin{itemize}
\item \textsuperscript{5}Sec. 139 ibid.
\item \textsuperscript{6}Sec. 153 ibid.
\item \textsuperscript{7}Sec. 192 et. seq. ibid.
\item \textsuperscript{8}Sec. 207 et. seq. ibid.
\item \textsuperscript{9}Sec. 140A ibid.
\item \textsuperscript{10}Sec. 220 ibid.
\item \textsuperscript{11}Sec. 2 (31) ibid.
\end{itemize}
liability and not on behalf of its shareholders; the shareholders are separately liable to pay tax on their total incomes including the gross amount of dividends from the company.\(^\text{12}\)

The Companies Act divides companies into public companies and private companies; the latter being companies which restrict the right to transfer their shares, limit the number of their members to 50, and prohibit an invitation to the public to subscribe for their shares and debentures.\(^\text{13}\) The definition of 'company' under the Income-tax Act is much wider. Apart from companies registered under the Companies Act, it includes a statutory corporation, a body incorporated in a foreign country and even an unincorporated institution, association or body, whether Indian or non-Indian, which is declared by the Central Board of Direct Taxes to be a company for any particular assessment year.\(^\text{14}\) Within this wide definition, companies are divided into Indian companies, domestic companies and foreign companies. An 'Indian company'

\(^{12}\) Howrah Trading Co. Ltd. v CIT, 36 ITR 215 (SC) and Purshottamadas Thakurdas v. CIT, 48 ITR 206 (SC).

\(^{13}\) Sec. 3 of the Companies Act, 1956.

\(^{14}\) Sec. 2 (17) of the Income-tax Act, 1961.
is a company formed and registered in India. A 'domestic company' includes additionally a company which maintains its share register at its principal place of business in India, holds its general meeting for passing accounts and declaring dividends in India and pays all its dividends in India. A 'foreign company', is a company which is neither an Indian company, nor a domestic company.

C. Residence and Tax Liability: The extent of liability to tax depends not on domicile, or citizenship or nationality, but on residence of the tax-payer. The tax liability of a 'resident' person extends to his total world income, i.e., including income which accrues, arises, or is received outside India. The tax liability of a non-resident person extends to income accruing, arising or received in India.

An individual is 'resident' in India if he is in India for at least 182 days in the year or having been in India for at least 365 days in the preceding four years he is in India for at least 60 days in the

15 Sec. 2 (26) ibid.
16 Sec. 80B (2) ibid & Rule 27.
17 Sec. 80B (4) ibid.
18 Sec. 5 ibid. See infra for income statutorily deemed to accrue, arise or be received in India.
year. A company is 'resident' if it is an Indian company or if the control and management of its affairs is situated wholly in India. The words 'control and management' signify the controlling and directive power, the head and brain; and 'situated' implies the functioning of such power at a particular place with some degree of permanence. It has been held that the control and management of a company is ordinarily situated at the place where the directors' meeting are held. Factors like the holding of shareholders' meetings, the residence of directors or even the place where business operations are actually carried on, are not decisive.

D. Computation of Business Income: Income from profits and gains of business is computed on ordinary commercial principles and in accordance with the method

19 Sec. 6 ibid.
20 Subbavva Chettiar v. CIT, 19 ITR 168 (SC)
21 Narottam and Pereira Ltd. v. CIT, 231 ITR 454.
22 Stanley v. Gramophone & Typewriters Ltd., 5 T.C. 358 (CA).
24 Erine Estate v. CIT, 34 ITR 1 (SC)
25 Badridas Daga v. CIT, 34 ITR 10 (SC)
of accounting regularly employed by the tax-payer. 26 The Act specifically mentions some of the allowable expenses like rents, rates, taxes, repairs and insurance 27 and then goes on to lay down a general principle that any expenses incurred by the tax-payer during the year wholly and exclusively for the purpose of business shall be allowed if these are not in the nature of personal expenses of the tax-payer or in the nature of capital expenditure. 28 The Act does not define 'capital expenditure' but it has generally been held that expenditure incurred with a view to bringing into existence an asset or advantage for the enduring benefit of a trade is ordinarily of the nature of capital expenditure. 29 In the case of a business of prospecting for or extraction or production of mineral oils carried on in association with Government or their nominee, the Act empowers the Government to provide by agreement for the making of special allowances in respect of infructuous or abortive explo-

26 Sec. 145 ibid.
27 Sec. 30 et seq. ibid.
28 Sec. 37 ibid. For capital expenditure on scientific research, however, see p. 15 infra.
ration expenses or depletion of mineral oils, in lieu of or in addition to the allowances admissible under the Act. 30

The following expenses are not, however, allowed to the extent indicated below:

1. Entertainment expenditure beyond a certain limit. 31

2. Expenditure incurred on advertisement in any souvenir, brochure, tract, pamphlet or the like published by a political party. 32

3. Expenditure incurred on the maintenance of a guest house. 33

4. Twenty per cent of the expenditure on advertisement, publicity or sales promotion. 34

5. Expenditure in the nature of 'head office expenditure' comprising executive and general administration expenditure incurred by a non-resident taxpayer outside India to the extent such expenditure exceeds five percent of the Indian income for the year or the yearly average of such expenditure allowed during the years 1974 to 1976 whichever is less. 35

6. Interest or salary payable outside India on which tax has not been paid or withheld or arranged for. 36

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30 Sec. 42 ibid.

31 The limit is computed at 1/2% of the first Rs. one million of profits, 1/4% of the next Rs. four million of profits and 1/8% of the remaining profits subject to a maximum of Rs. 50,000 in all. (Sec. 37 (2A) ibid).

32 Sec. 37 (2B) ibid.

33 Sec. 37 (4) ibid.

34 Such expenditure incurred by domestic companies outside India in connection with export activities is allowed in full. (Sec. 37 (3A) ibid).

35 Sec. 44C ibid.

36 Sec. 40 (a) (i) & (iii) ibid.
7. Any payment made on account of income-tax or wealth-tax. 37

8. Travel expenditure in excess of the limits laid down in Rule 6 D.

9. Expenditure on the provision of any remuneration, benefit or amenity to or the user of any asset of the company by a director of the company or a person who has a substantial interest 38 in the company or a relative of such director or person in so far as such expenditure exceeds Rs. 72,000 per annum per person. 39

10. Similar expenditure on payment of salary or perquisites 40 to an employee, other than a foreign technician, in so far as such expenditure exceeds Rs. 5,000 per month in respect of salary and 1/5 of salary or Rs. 1,000 per month in respect of perquisites. 41

2. Rates of Tax: The rates of tax are laid down in the Annual Finance Act every year. The rates applicable to

37 Sec. 40 (a) (ii) & (iia) ibid.

38 A person has a substantial interest in a company if he is the beneficial owner of equity capital carrying not less than 20% of the voting power. (Explanation below sec. 40A (2) (ibid)).

39 Sec. 40 (c) ibid.

40 'Perquisite' means provision of accommodation free of rent or at a concessional rent, provision of any benefit or amenity free of cost or at a concessional rate and payment for any obligation of the employee or for any life insurance policy or contract of annuity on his behalf (Explanation 2 (b) under Sec. 40A (5) ibid).

41 Sec. 40A (5) ibid.
to companies for the assessment year 1984-85 are given in the following table:

<table>
<thead>
<tr>
<th>Type of Company</th>
<th>Rate as percentage of total income</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic 42</td>
<td></td>
</tr>
<tr>
<td>a) widely held 42</td>
<td>55</td>
</tr>
<tr>
<td>b) Closely held 43</td>
<td></td>
</tr>
</tbody>
</table>

42 A company is 'widely held' if:-

(i) not less than 40% of its shares are held by Government or the Reserve Bank of India or a corporation owned by that Bank; or

(ii) it is a charitable or other company registered under Section 25 of the Companies Act, 1956; or

(iii) it is a company having no share capital and being declared by an order of the Central Board of Direct Taxes to be a widely held company, or

(iv) it is a public company and either its shares are listed in a recognized stock exchange in India, or its equity shares carrying not less than 50% (40% in the case of an industrial company) of the voting power are held unconditionally throughout the year by Government or a statutory corporation or a widely held company or a subsidiary of such company.

43 A company not satisfying the above conditions is a 'closely held' company.
Industrial 60
Others 65

Foreign

(a) Royalties and technical fees received from Indian concerns in pursuance of agreements made before 1 April, 1976 and approved by the Government of India.

(b) Balance of total income 70

The amount of income tax calculated at the above rates is increased by a surcharge at the rate of 5% of such income-tax.\(^45\) The amount of surcharge may, however, be reduced to half if deposit of an equal amount is made with the Industrial Development Bank of India.\(^46\)

From 1 April, 1976 incomes of foreign companies from dividends, royalties, technical fees and interest.\(^47\)

\(^44\) 'Industrial company' means a company which is mainly engaged in the business of generation and distribution of electricity or any other form of power or carriage, by road or inland waterways, of passengers or goods or in the construction of ships or in the execution of projects or in the manufacture or processing of goods or in mining.

\(^45\) Part III of the First Schedule to the Finance Act, 1983.

\(^46\) Section 2 (7) of the Finance Act, 1983.

\(^47\) Sec. 57 of the Income-tax Act, 1961.

\(^48\) Sec. 44D ibid.
received from Government or Indian concerns are taxed on gross basis i.e. without allowing any deduction for any expenditure incurred in connection with their earning, but at the reduced rates given in the following table. The tax is withheld at source.

**TABLE**

**RATES OF TAX ON DIVIDEND ROYALTY AND TECHNICAL FEES**

<table>
<thead>
<tr>
<th>Type of income</th>
<th>Rate of tax as percentage of income</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dividends</td>
<td>25</td>
</tr>
<tr>
<td>Interest</td>
<td>25</td>
</tr>
<tr>
<td>Royalty consisting of lump sum consideration for transfer or imparting of information outside India in respect of any data, documentation, drawing or specification relating to any patent, invention etc.,</td>
<td>20</td>
</tr>
<tr>
<td>Other royalty income</td>
<td>40</td>
</tr>
<tr>
<td>Fees for technical services</td>
<td>40</td>
</tr>
</tbody>
</table>

Capital gains are divided into long-term capital gains and short-term capital gains depending upon the fact whether the asset transferred had or had not been held by the taxpayer for more than 3 years preceding
its transfer. Short-term capital gains are taxed like any other income. Long-term capital gains are given a concessional treatment as under:

(a) Gains relating to buildings or lands -
   In the case of widely held companies whose income excluding such capital gains does not exceed ₹1,00,000
   40%
   In other cases -
   50%
(b) Gains relating to other assets
   40%

Some of the more important tax benefits are mentioned below:

1. Depreciation: The Indian Income-tax Act contains extensive provisions allowing depreciation in respect of buildings, machinery, plant and furniture owned by the tax-payer and used by him during any part of the year for the purpose of his business. Different percentages of depreciation allowance varying from 2.5% to

49 Sec. 2 (42A) ibid.
50 Sec. 115 ibid.
51 Sec. 32 and 34 ibid read with Rule 5.
100% in the case of buildings and from 5% to 100% in the case of plant, machinery and furniture are laid down in Appendix I to the Income-tax Rules, 1962. Depreciation at these rates is allowed on the written down value of the assets mentioned i.e. on their actual cost less depreciation allowed in the earlier years. For ocean going ships, however, depreciation is allowed on the straight line method i.e. on the actual cost. The word 'plant' is defined to include ships, vehicles, books, scientific apparatus and surgical equipment. It has been interpreted in a wide sense to include things like sanitary and pipeline fittings, railway sidings, and safe deposit vaults.

b. Additional Depreciation: Additional depreciation is allowed in the following cases:

52 The general rate of depreciation for non-specified plant and machinery is 15%.
53 Sec. 43 (3) ibid.
54 CIT v. Taj Mahal Hotel, 82 ITR 44 (SC).
55 Kalinga Tubes Ltd. v. CIT, 96 ITR 2 0.
56 CIT v. Union Bank of India Ltd., 102 ITR 280.
(i) In respect of new machinery or plant (except ships, aircrafts, road transport vehicles and office appliances and machinery or plant installed in any office premises or residential accommodation) including reconditioned machinery or plant imported from outside India, installed after 31 March, 1980 but before 1 April 1985, additional depreciation allowance is given at 50 per cent of the normal depreciation. This additional allowance is given only in the first year.

(ii) In respect of machinery and plant, whenever installed by an Indian company in an approved hotel, an additional depreciation allowance is given at 50 per cent of the normal allowance. This additional allowance is given year after year.

C. Initial Depreciation: Initial depreciation allowance is given in the first year in the following cases:

(i) At 40 per cent in the case of a new building used solely for the residence of low-paid employees or for the welfare of such employees as a hospital, creche, school, canteen, library, recreation centre, shelter, restroom or lunchroom.

57 Sec. 32 (1) (iia) of the Income-tax Act, 1961
(ii) At 25 per cent in respect of new building owned by an Indian company and used as an approved hotel. 50

d. Extra-shift Allowance: In the case of a concern that has worked double or triple shift at any time during the year an extra-shift allowance is given on machinery and plant in addition to the normal depreciation allowance at 50 per cent of the normal allowance for double shift working and 100 per cent of the normal allowance for triple shift working. Where the extra-shift is worked only during a part of year the extra-shift allowance is given on a pro-rata basis. Certain items of plant and machinery like locomotives, electric fittings and switchgear are however, specifically marked in Appendix I to the Income-tax Rules as not eligible for the extra-shift allowance.

e. Carry Forward: If the profits in any particular year are not sufficient to absorb the entire depreciation allowance that is admissible the balance amount is allowed to be carried forward indefinitely to be set off against the profits of future years. 61

50 Sec. 32 (ii) (v) ibid.
61 Sec. 32 (2) Ibid.
f. Balancing Allowance/Charge: The sum total of all these allowances should not ultimately exceed the actual cost to the tax-payer of the particular asset. If the asset is, at any stage, sold, discarded, demolished or destroyed, the excess of the written down value over the amounts realized together with the scrap value is allowed as a balancing allowance. 62 In the converse situation, where the amount realized and the scrap value exceed the written down value, the excess is brought to tax as income. 63

g. Amortization of Other Assets: The depreciation allowance is given only in respect of the assets specified above. There are, however, separate provisions allowing amortization of capital expenditure in the following cases:—

(i) Cost of patent rights or copyrights is allowed to be amortized over a period of fourteen years. 64

(ii) Capital expenditure incurred for promoting family planning among employees is allowed to be amortized over a period of five years. 65

62 Sec. 32 (1) (iii) ibid.
63 Sec. 41 (2) ibid.
64 Sec. 35A ibid.
65 Sec. 36 (1) (ix) ibid.
(iii) In the case of Indian companies, preliminary expenses incurred prior to the setting up of the business and expenses incurred before the commencement of commercial production on prospecting for any of the minerals specified in the Seventh Schedule to the Act may be amortized over a period of ten years.

2. Investment Allowance

In respect of a new ship, aircraft, machinery or plant (including a used ship or aircraft or reconditioned machinery or plant imported from abroad) an investment allowance at the rate of 25 per cent of the actual cost is allowed in the first year. The allowance is not given in respect of plant or machinery used in the production of certain low priority articles specified in the Eleventh Schedule to the Act.

This allowance is conditional on an amount equal to 75 per cent of the investment allowance (50 per cent in the case of ships) being debited to the profit and loss account of the business and credited

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66 Sec. 35D and 35E ibid.

67 Sec. 32A and 155 ibid.
to a special reserve account to be utilized within a period of ten years for acquiring new ship, aircraft, plant or machinery. During this period of ten years the investment allowance reserve must be utilized for the business other than for distribution by way of dividends or profits or for remittance outside India. If the ship, aircraft, machinery or plant in respect of which investment allowance is given is transferred by the taxpayer to any other person (other than Government, a local authority or a Government company or corporation) otherwise than under a scheme of amalgamation before the expiry of eight years of if new ship, aircraft, machinery or plant is not acquired within ten years or the special reserve is utilized for a forbidden purpose during that period the investment allowance is withdrawn.

If the profits of the year are not sufficient to absorb the admissible amount of investment allowance the balance amount can be carried forward and set off against profits of future years upto eight succeeding assessment years.

3. Development Allowance

A tax-payer carrying on the business of growing and manufacturing tea in India is given a development

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68 Sec. 33A ibid.
allowances at the rate of 50 per cent of the cost of planting tea bushes on virgin land or on land previously abandoned. The cost of planting for this purpose is limited to a range of Rs. 30,000 to Rs. 40,000 per hectare. The allowance is conditional on the creation and utilisation of a special reserve and the non-transfer of the planted land over a period of eight years as in the case of investment allowance.

4. Tax Holiday

a. New Investment: A company setting up a new hotel, or acquiring a new ship, or starting with new machinery or plant or reconditioned machinery or plant imported from outside India, an industrial undertaking not producing low priority articles listed in the Eleventh Schedule to the Act, is given a partial tax holiday to the extent of 25 per cent of the profits from such new investment for a period of seven years. The concession in respect of new hotels and ships is confined to Indian companies.69

b. Backward Areas: A tax-payer setting up a new industrial undertaking or an approved hotel in a backward area70 in the country is given a partial

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69 See 80 ibid.

70 A list of backward areas is given in the Eighth Schedule to the Income-tax Act.
tax holiday to the extent of 20 per cent of the profits of such undertaking or hotel for a period of ten years.\textsuperscript{71}

c. Free Trade Zones: A tax payer deriving profits and gains from an industrial undertaking set up in the Kandla Free Trade Zone or Santa Cruz Electronics Exports Processing Zone or any other free trade zones that may be set up in India is allowed full tax holiday in respect of such profits and gains for a period of five years. In such cases the normal tax concessions mentioned above are not admissible but the tax-payer may opt for them in lieu of this concession if such option is more beneficial to him.\textsuperscript{72}

5. Expenditure on Scientific Research:

In respect of expenditure on research and development the following special concessions are allowed.

a. Revenue as well as capital expenditure incurred in the year on scientific research related to the tax-payer's business is allowed in full. Capital expenditure as well as revenue expenditure on payment of salaries to research personnel or on material inputs incurred during a period of 3 years

\textsuperscript{71}Sec. 80 HH ibid.

\textsuperscript{72}Sec. 10A ibid.
preceding the commencement of business are also allowed in full in the year of commencement of business.

b. Donations to approved scientific research associations, universities, colleges or other institutions to be used for scientific research are allowed deduction in full.

c. In respect of expenditure incurred on sponsored research in approved laboratories a weighted deduction equal to 1 1/3 times of the actual expenditure is allowed.

d. In respect of expenditure incurred on an approved research programme in any approved inhouse research and development unit a weighted deduction equal to 1 1/4 times of the actual expenditure is allowed. 73

6. Export Turnover

Indian companies exporting goods or merchandise, other than agricultural commodities, mineral oil, minerals and ores, are allowed a deduction equal to one per cent of their export turnover for

73 Sec. 35 ibid.
the year plus five per cent of the amount by which
the export turnover for the year exceeds the export
turnover of the immediately preceding year.\textsuperscript{74}

7. \textbf{Technical Fees}

Any income derived by an Indian company from
a foreign government or enterprise by way of royalty,
commission, fees or any other payment for the transfer of technical know-how under an agreement approved
by the Central Board of Direct Taxes is fully exempt.
Where shares of a foreign company are allotted to an
Indian company in consideration of the transfer of
technical know-how by the Indian company to such
foreign company, 100 per cent of the dividend income
from such shares is exempt from tax.\textsuperscript{75}

8. \textbf{Intercompany Dividends}

A domestic company is allowed the following
concessions in respect of its income from dividends:

a. Dividend income from an Indian company
engaged in the manufacture or production
of the following articles is fully exempt:

- Non-ferrous metal,
- Ferro-alloys and special steels,
- Steel castings and forgings,
- Electric motors,

\textsuperscript{74}Sec. 80 HHC.

\textsuperscript{75}Sec. 80N and 80'O ibid.
Industrial agricultural and earthmoving machinery,
Machine tools,
Fertilisers,
Soda ash,
Caustic soda,
Commercial vehicles,
Ships,
Tyres and tubes,
Paper, pulp and newsprint,
Cement,
Pesticides,
Organic and inorganic heavy chemicals,
Synthetic rubber and rubber chemicals,
Industrial explosives,
Basic drugs,
Electronic components and raw materials.

b. Dividend income from any other domestic company is exempt to the extent of 60 per cent of such income.

9. **Ceiling on Incentives**

The sum total of deductions on account of tax incentives, other than depreciation and tax holiday in Free Trade Zones, is not allowed to exceed 70 per cent of the total income computed before allowing such deductions. The balance amounts of deductions, if any, can however be carried forward and claimed in future years.

10. **Carry Forward of Losses**

Business losses of one year are allowed, so long as the particular business is not closed down,

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76 Sec. 80 M ibid.
77 Sec. 80 VWA ibid.
to be carried forward and set off against any business profits of the taxpayer in future years upto eight succeeding assessment years.\textsuperscript{78} Similarly, short-term and long-term capital losses are separately allowed to be carried forward and set off against future short-term and long-term capital gains respectively upto eight assessment years.\textsuperscript{79}

G. International Aspects: The following provisions are of special interest to foreign investors.

1. Taxation at Source

It has been mentioned that the tax liability of a non-resident person extends only to income accruing, arising or received in India including income deemed to accrue or arise or be received in India. In the following cases income is deemed to accrue or arise in India.

(i) Income accruing or arising directly or indirectly through or from any property in India or any asset or source of income in India or the transfer of a capital asset situated in India.

(ii) Income from any dividend paid by an Indian company outside India.

(iii) Income accruing or arising directly or indirectly through or from any business connection in India.

In the case of a business of which all the operations are not carried out

\textsuperscript{78}Sec. 72 ibid.

\textsuperscript{79}Sec. 74 ibid.
in India, it is only the income which is attributable to the operations carried out in India which is deemed to arise in India. No income is deemed to accrue or arise in India to a non-resident, from operations which are confined to the purchase of goods in India for the purpose of export or, in the case of a news agency or publisher of newspapers, magazine or journals, from collection of news and views in India for transmission outside India.

The Act gives no definition of the phrase 'business connection'. It has been held to involve a relation between a business carried on by a non-resident which yields profits or gains and some activity in India which contributes directly or indirectly to the earning of those profits or gains. It would include a branch, factory, agency, receivership or management. Thus where a non-resident sells goods in India through an agent and the agent pays tax on his commission, a portion of the non-resident principal's profits on those sales is taxable on the doctrine of business connection. But where a non-resident sells goods from abroad to an Indian importer no income is deemed to accrue or arise to the non-resident from such sale even if the non-resident is the parent company and the Indian importer

80 CIT v. Aggarwal & Co., 56 ITR 20 (SC)
82 Abdullabhai Abdul Kadar v. CIT, 22 ITR 241.
its subsidiary as long as the contract of sale is made outside India and the sale is on a principal-to-principal basis.83

(iv) Incomes by way of interest, royalty and fees for technical services payable by
- Government, or
- A resident person except in connection with a business or profession or a source of income of such person outside India, or
- A non-resident person in respect of a business or profession or source of income of such person in India.84

2. Foreign Shipping Lines

In the case of non-resident shipping lines tax is levied at 7 1/2 per cent of the gross amounts:

- Paid or payable whether in India or abroad on account of the carriage of passengers, livestock, mail or goods shipped at any Indian port, and
- Received or deemed to be received in India on account of the carriage of the said things shipped at any port outside India.85

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84 Sec. 9 of the Income-tax Act, 1961.

85 Sec. 44B ibid.
3. Business of Prospecting for or Extraction of Mineral Oils

If a foreign company carries on a business of prospecting for or extracting or producing mineral oils including petroleum and natural gas in association with Government or their nominee, the profits and gains of such business are taxed at a lower rate of 55 per cent plus a surcharge of 2 1/2 per cent of tax. The other income if any of such a company is taxed at the average rate of tax.  

4. Vicarious Liability of Indian Agent

In respect of income deemed to accrue or arise in India to a non-resident, the act places a vicarious personal liability on the agent of the non-resident in India. If there is no such agent any person in India who is employed by or on behalf of the non-resident or who has any business connection with the non-resident or from or through whom the non-resident is in receipt of any income or who is the trustee of the non-resident or who has acquired, by means of a transfer from the non-resident, a capital

86 Government of India, Ministry of Finance "Notification No. G.S.R. 306 (a) of 31 March, 1933", issued under Section 293A ibid.


asset in India, is statutorily treated as an agent of
the non-resident in India. 89

5. **Non-resident Partner**

The tax on the share income of a non-resident
partner of a partnership firm is assessed on the
firm at the rates applicable to such partner and is
payable by the firm. 90

6. **Diversion of Income to Non-resident**

where, in a business carried on between a
resident and a non-resident, it appears that owing
to the close connection between them, the course of
business is so arranged as to result in sub-normal
profits to the resident, the resident may be liable
to tax in respect of profits which he has not, in
fact made but which he might reasonably be expected
to have made had he done the business on ordinary
commercial terms. 91

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89 Sec. 163 ibid.
90 Sec. 182 ibid.
91 Sec. 92 ibid. See also Kanga & Palkhivala,
7. Tax Treaties

The Government of India have powers under the Act to enter into agreements with foreign countries for grant of relief in respect of double taxation, for avoidance of double taxation, for exchange of information for prevention of tax evasion/avoidance and for recovery of tax. In exercise of this power Government have entered into tax treaties with the following countries:

<table>
<thead>
<tr>
<th>Comprehensive</th>
<th>Limited to aircrafts and shipping profits</th>
<th>Limited to shipping profits</th>
<th>Limited to aircrafts profits</th>
</tr>
</thead>
<tbody>
<tr>
<td>2. Belgium</td>
<td>2. Czechoslovakia</td>
<td>2. Ethiopia</td>
<td>2. Iran</td>
</tr>
<tr>
<td>3. Denmark</td>
<td>3. German Democratic Republic of Germany</td>
<td>3. Iran</td>
<td>3. Italy</td>
</tr>
<tr>
<td>5. France</td>
<td>5. Poland</td>
<td>5. Lebanon</td>
<td>5. Switzerland</td>
</tr>
<tr>
<td>6. Greece</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. Japan</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>8. Libya</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>9. Malaysia</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>10. Norway</td>
<td></td>
<td></td>
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<tr>
<td>11. Singapore</td>
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<td></td>
<td></td>
</tr>
</tbody>
</table>

92 Sec. 90 ibid.
13. Sri Lanka (Revised)
14. Sweden
15. Tanzania
16. United Arab Republic
17. United Kingdom

India is also negotiating with several other countries for concluding tax treaties. Treaties with the following countries are already in an advanced stage:

<table>
<thead>
<tr>
<th>Comprehensive</th>
<th>Limited to aircrafts profits</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Italy</td>
<td>1. Kuwait</td>
</tr>
<tr>
<td>2. Mauritius</td>
<td>2. Australia</td>
</tr>
<tr>
<td>4. Belgium (Revised)</td>
<td></td>
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<tr>
<td>5. Canada</td>
<td></td>
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<tr>
<td>6. Federal Republic of Germany (Revised)</td>
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<td>7. Finland (Revised)</td>
<td></td>
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<tr>
<td>8. Kenya</td>
<td></td>
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<tr>
<td>9. Syria</td>
<td></td>
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<tr>
<td>10. Thailand</td>
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</tr>
</tbody>
</table>

The following are some of the broad features of these treaties.94

a) Business profits: Industrial and commercial profits attributable to a 'permanent establishment' would be taxed by the country in which such 'permanent establishment' existed.

94 See N.B. Rao, Double Tax Treaties between Developed and Developing Countries, (New Delhi, 1983), Chapter IX.
establishment' is located; the other country would give relief by way of tax credit or exemption.

There is no uniform definition of 'permanent establishment'. Thus, a sales exhibition is included in some cases and not included in others. A construction, installation or assembly project is included in some cases without any time limit, in others with a time limit of 90 days, and in still others with a time limit of 6 months.

b) Aircrafts and shipping: In the case of aircrafts tax jurisdiction is given uniformly to the country of residence only. In the case of shipping, however, tax jurisdiction is given to both countries; each country would tax profits arising in that country but would reduce the tax chargeable by 50 per cent (2/3rd in some cases) in respect of income arising out of operation of ships belonging to entities resident in the other country. The other country would give relief by credit or exemption for the reduced amount of tax so charged.

c) Investment incomes (dividends, interest and royalty): Tax jurisdiction is given in all cases to the country of source, the other country would provide relief by way of tax credit or exemption. In some cases such relief would extend also to the tax spared.
d) Other matters: All agreements embody the arms length principle and contain provisions for exchange of information and mutual assistance. A non-discrimination clause appears in some of the agreements.

8. Unilateral Relief

The Act also provides for unilateral relief in the case of resident taxpayers in respect of their foreign incomes which have been taxed both in India as well as foreign countries. Relief is given on the doubly taxed income at the Indian rate of tax or the rate of tax of the foreign country whichever is lower. 95

9. Special Exemptions

i. The income of a non-resident from interest on, or from premium on the redemption of, any bonds issued by the Government or by an industrial undertaking or financial corporation in India under a loan agreement made or guaranteed by the Government with the International Bank for Reconstruction and Development or the Development Loan Fund of the

95 Sec. 91 of the Income-tax Act, 1961.
United States of America is totally exempt from tax. 96

ii. So also the income from interest 97 payable by Government or a local authority or the Industrial Finance Corporation of India, the Industrial Development Bank of India, the Export Import Bank of India and the Industrial Credit and Investment Corporation of India on foreign loans or by an industrial undertaking in India on—

a. loans raised from the International Finance Corporation, Washington, the Export Import Bank of Washington, the Export Import Bank of Japan, the Development Loan Fund, Columbia, the Kreditanstalt fur Wiederaufbau (West German Bank for Reconstruction) and the Banque Francaise due Commerce Exterior, Paris, 98 or

b. loans raised or debits incurred directly or through a financial institution or bank in India for purchase, outside India, of raw materials, components, or capital plant and machinery, or

96 Sec. 10 (4) ibid.
97 Sec. 10 (15) ibid.
c. moneys borrowed in any foreign currency under a loan agreement approved by the Government of India. 99

ili. The remuneration of a foreign technician serving in India in the employment of Government or a local authority or a statutory corporation or an approved scientific research institution or a business carried on in India, under a contract of service approved by the Government of India, is exempt from tax for a period of 24 months to the extent such remuneration does not exceed Rs. 4,000 per month. In respect of the remuneration in excess of Rs. 4,000 per month or beyond the period of 24 months (upto another 24 months), the exemption is available for tax, if any, paid by the employer on the non-exempt remuneration of the foreign technician. 101

99 The exemption in respect of (b) and (c) is limited to the rate of interest approved by Government.

100 Foreign technician' is a person having specialised knowledge and experience in constructional or manufacturing operations or in mining or in the generation or distribution of electricity or any other form of power or in agriculture, animal husbandry, dairy farming, deep sea fishing, ship building or such other field as the Government of India may specify (Explanation under Sec. 10 (6) (viia ibid).

101 Sec. 10 (6) (viia) ibid.
H. Re-assessment, Penalties, Prosecution and Appeals:
In the event of any income escaping assessment to tax in any year the Income-tax authorities can re-open the assessment of a particular year within periods ranging from four to sixteen years depending upon the amount of income escaping assessment and the fact whether or not such escape is caused by any omission or failure on the part of the taxpayer. 102 A default in complying with the provisions of the Income-tax Act may involve the taxpayer not only in penal consequences but also prosecution. 103

A taxpayer who is aggrieved by an order made by an Income-tax authority may move the same or a higher departmental authority as the case may be in rectification, 104 revision 105 or appeal 106 proceedings. A second appeal may be taken to an extra-

102 Sec. 147 et. seq. ibid.
103 Chapters XXI and XXII ibid.
104 Sec. 154 ibid.
105 Sec. 264 ibid.
106 Sec. 246 et. seq. ibid.
departmental Appellate Tribunal.\textsuperscript{107} The Tribunal is the final fact-finding authority but on questions of law a reference may also be made to the High Court,\textsuperscript{108} or in the event of divergence of opinion between various High Courts on a particular point, to the Supreme Court of India.\textsuperscript{109} From a judgement of a High Court delivered on such a reference also an appeal can be taken to the Supreme Court of India.\textsuperscript{110} Independently of these provisions a taxpayer can also move directly a High Court in writ proceedings under Article 226 of the Constitution, or where he can allege a breach of any of his fundamental rights, even the Supreme Court of India under Article 32 of the Constitution.

\textbf{Surtax}

\textit{A. General:} Surtax is levied under the \textit{Companies (Profits) Surtax Act 1964} and the \textit{Companies (Profits) Surtax Act 1964}.

\begin{itemize}
  \item \textsuperscript{107} Sec. 253 et seq. ibid.
  \item \textsuperscript{108} Sec. 256 ibid. A High Court is the highest Court of Judicature in a State.
  \item \textsuperscript{109} Sec. 257 ibid.
  \item \textsuperscript{110} Sec. 261 ibid.
\end{itemize}
fit's) Surtax Rules, 1964 made thereunder. This act also applies to the Exclusive Economic Zone of India with regard to the prospecting for or extraction or production of mineral oils or the provision of any services or facilities, ships, aircraft, machinery or plant, in connection therewith. Foreign companies carrying on such activities in the Exclusive Economic Zone in association with the Government or their nominee are, however, exempted. 111

B. Chargeable profits: The tax is charged on chargeable profits of a company to the extent they exceed a 'statutory deduction' which is defined as an amount equal to 15 per cent of the capital of the company on the first day of the accounting year or an amount of Rs. 200,000 whichever is more. 112

111 Government of India, Ministry of Finance, Notifications Nos. 305 (n) and 307 (n) of 31 March, 1983 issued under Section 7 of the Territorial Waters, Continental Shelf, Exclusive Economic Zone and Other Maritime Zones Act, 1976 and Section 24AA of the Companies (Profits) Surtax Act, 1964.

112 Sec. 2 and 4 of the Companies (Profits) Surtax Act, 1964.
The chargeable profits are computed in the manner laid down in the First Schedule to the Act which broadly contemplates exclusion from the total income of certain items like:

i) Capital gains

ii) 50 per cent of the donations made to certain national funds and charitable institutions. 113

iii) Income from dividends of a domestic company.

iv) Income by way of royalties received from Government or a local authority or an Indian concern.

v) In the case of a foreign company, income by way of any interest or fees for rendering technical services received from Government or local authority or any Indian concern.

vi) Income tax payable for the year.

C. Capital: 'Capital' for the purpose of working out statutory deduction is computed in the manner laid down in the Second Schedule to the Act. Broadly, this includes paid-up share capital

113 50 per cent of these donations are excluded from the total income computed for income-tax itself on the conditions laid down in Section 80J of the Income-tax Act, 1961.
together with share premium and reserves other than fictitious reserves or mere provisions. To distinguish between a reserve and a provision, it has been held that a 'provision' should be taken to mean monies set aside out of the profits in any year to meet any known liability the amount of which cannot be quantified with substantial accuracy, whereas a 'reserve' would mean amounts set aside out of the profits and other surpluses which are not designed to meet any liability, contingency, commitment or diminution in the value of assets known to exist as on the date of the balance sheet.\(^{114}\) For the computation of capital on the first day of the accounting year it has been held that any addition to reserves sought to be made by the Board of Directors out of the profits of any particular year would, immediately on being approved at the annual General Meeting of the shareholders, become part of the reserves of the company with effect from the first day of the

\(^{114}\) Indian Steel and Wire Products Ltd. v. CIT, 42 Tax 1.
immediately following accounting year. 115

D. Rates of tax: The rate of tax is 25 per cent on so much of the chargeable profits as do not exceed 5 per cent of the capital of the company and 40 per cent on the balance. In the case of a widely held domestic company or a wholly owned subsidiary of such a company whose paid-up share capital is not less than 25 per cent of its capital computed for the statutory deduction, the amount of surtax is so limited as to ensure that the sum total of income tax and surtax does not exceed 70 per cent of the total income as computed for income tax. 116

Interest Tax

Interest tax is levied under the Interest Tax Act, 1974 and the Interest Tax Rules 1974 made thereunder, at the rate of three and half per cent of the chargeable interest of a banking company. The 'chargeable interest' means interest on loans and advances made in India including

115 CIT v. Mysore Electrical Industries Ltd. 80 ITR 566(Sc).

116 Third Schedule to the Companies (Profits) Surtax Act, 1964.
commitment charges other than interest on Government securities, interest on debentures or other securities of local authorities, companies or statutory corporations and interest on loans and advances made to other banks. 117

Wealth Tax

Wealth tax is levied, under the Wealth Tax Act, 1957 and the Wealth Tax Rules, 1957 made thereunder, on the net wealth comprising the excess of the aggregate value of assets over the aggregate value of liabilities of the taxpayer on the last day of preceding year.

The wealth tax is not levied on widely held companies. In the case of closely held companies wealth tax is levied at two per cent only in respect of net wealth comprised in their non-productive assets like jewellery, land, residential buildings and motor cars. 118

Gift-Tax

Gift tax is levied, under the Gift Tax Act, 1958 and the Gift Tax Rules, 1958 made thereunder,

117 Sec. 2 (7) and 5 of the Interest Tax Act, 1974.

118 Sec. 40 of the Finance Act, 1933.
on the sum total of all gifts made by the tax-payer during the preceding year.\textsuperscript{119} The rates of tax are on a graduated scale varying from 5 per cent on gifts not exceeding Rs. 20,000 to 75 per cent on gifts exceeding Rs. 2 million.\textsuperscript{120} The applicable rate is, however, based on the aggregate value of all gifts made in the preceding 5 years.\textsuperscript{121}

A gift is defined to mean the transfer by one person to another of any existing moveable or immoveable property made voluntarily and without consideration in money or money's worth.\textsuperscript{122} The word 'transfer' is given a wide meaning to include any disposition, conveyance, assignment, settlement, delivery, payment or other alienation of property as well as the creation of a trust in property, the grant or creation of any lease, mortgage, charge, easement, licence, power, partnership or interest in property, the exercise of a power of appointment of property, the\textsuperscript{123}\textsuperscript{124} power vested in any person and in general, any other transaction entered

\textsuperscript{119} Sec. 3 of the Gift-tax Act, 1958.
\textsuperscript{120} Schedule to the Act ibid.
\textsuperscript{121} Sec. 6A ibid.
\textsuperscript{122} Sec. 2 (xii) ibid.
into with intention to diminish, directly or indirectly, the value of the property of the transferor and increase the value of the property of the transferee. 123

Public companies and their subsidiaries are exempt from gift tax if shares carrying more than 50 per cent of the total voting power in the company were not, at any time during the year, controlled or held by less than 6 persons. 124

Estate Duty

Estate Duty is levied under the Estate Duty Act, 1953 and the Estate Duty Rules, 1953 made thereunder. The duty is levied on the principal value of the estate passing on the death in India of a person, irrespective of the domicile, nationality or residence of such person. Immovable property located outside India is, however exempt. In the case of a person who was not domiciled in India at the time of death moveable property located outside India is also exempt. 125

123 Sec. 2 (xxiv) ibid.
124 Sec. 45 ibid.
125 Sec. 21 of the Estate Duty Act.
A company incorporated outside India and carrying on business in India, which has been treated as resident for income tax purposes in two out of the three preceding years, is liable for the estate duty payable on the principal value of the shares or debentures held in the company by a deceased person who was not domiciled in India. The rate of duty in such a case is 7 1/2 per cent of the principal value.

The preceding five taxes, surtax, interest tax, wealth tax, gift tax and estate duty are also administered by the Central Board of Direct Taxes. The general and procedural provisions mentioned under income tax apply, mutatis mutandis, to these taxes.

Duties of Excise

A. General: Duties of excise and customs constitute the most important indirect taxes in India. Together they account for 77 per cent of the total tax revenues of the Government of India.  

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126 Sec. 20A ibid.

These are administered by the Central Board of Excise and Customs set up under the Central Boards of Revenue Act, 1963 within the Ministry of Finance.

**B. Central Excise Tariff**: Central excise duties are levied under the Central Excises and Salt Act, 1944 and the Central Excise Rules, 1944 made thereunder. The duties are neutral as between Indian and foreign companies. A list of excisable goods is given in the first Schedule to the Act which is commonly referred to as the Central Excise Tariff. The tariff is comprehensive in so far as it includes a residuary item entitled, 'All other goods, not elsewhere specified'.

The rates of duty given in the Tariff are mostly on ad valorem basis; in some cases there are specific rates i.e., rates fixed per unit of weight, volume, length or area. In either case, the rates

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128 Levy of excise duty on alcoholic liquors for human consumption and on opium, Indian hemp and other narcotic drugs and narcotics not including medicinal and toilet preparations containing these substances, falls in the State List of subjects in the Constitution of India and excise duties on these goods are levied under different State Acts. Excise duties on medicinal and toilet preparations are levied by the Centre under the Medicinal and Toilet Preparations (Excise Duties) Act, 1955 but collected and retained by the States in terms of Article 268 of the Constitution.

129 Item 68.
are often on a sliding scale according to different slabs of production or value. Since, however, the Central Government and, to a certain extent even the Central Board of Excise and Customs, have powers to allow general as well as specific exemptions, partial or total, the effective rates of duty, within the rates specified in the Tariff, are regulated from time to time by executive notifications.

C. Special Excise Duty: Apart from the basic excise duty a special excise duty is levied under the Annual Finance Act as a percentage of the basic duty. The rate of this duty under the Finance Act 1983 is 10 per cent. 131

D. Additional Excise Duties: Additional excise duty, in lieu of sales tax, is levied on sugar, tobacco and textiles under the Additional Duties of Excise (Goods of Special Importance) Act, 1957. 132

Additional duties of excise and cesses are also levied on some other commodities under various additional duties.

130 Rule 8.
131 Sec. 54 of the Finance Act, 1983.
132 Kamlapathi Tripathi Committee has recommended addition of five other commodities, vanaspati, medicines, cement, paper & petroleum to this list.
other Acts. 133

2. **Assessable value**: Where duty is leviable *ad valorem* the value determined for the purposes of duty is referred to as assessable value. In respect of certain goods like motor vehicles, internal combustion engines and electric wires, tariff values are fixed by the Central Government which are revised from time to time. In most cases, however, the assessable value is determined by the Excise authorities on the principle that it should be the normal price at which such goods are ordinarily sold in the course of whole-sale trade for delivery at the time and place of removal where the buyer is not

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a related person and the price is the sole consideration for the sale.\textsuperscript{134} The assessable value includes the cost of packing except such as is of durable nature and is returnable by the buyer but excludes the amount of excise duty itself, sales tax and other taxes if any as well as the normal trade discount.\textsuperscript{135}

E. \textbf{Export Goods} : The goods meant for export are exempt from excise duty.\textsuperscript{136} The manufacturer may either clear the goods on payment of duty and claim refund on exportation or he may remove the goods for export without payment of duty but subject to the execution of a bond with security/surety for a sum equivalent to the duty chargeable on such goods.\textsuperscript{137}

The manufacturer is also entitled to duty drawback under the Customs and Central Excise Draw-back Rules, 1971 in respect of duties of excise paid on inputs for the manufacture of export goods.\textsuperscript{138}

Capital goods components and raw materials supplied to 100 per cent Export Oriented Units and

\textsuperscript{134} Section 4 (a) of the Central Excises and Salt Act 1944.

\textsuperscript{135} Sec. 4 (d) ibid.

\textsuperscript{136} Rule 12

\textsuperscript{137} Rule 13

\textsuperscript{138} See p.14infra.
the finished products of such Units are also exempt from excise duty. So also goods supplied to industries in the Kandla Free Trade Zone and the Santa Cruz Electronics Export Processing Zone for use in the production of export goods.

G. Excise Control: Every manufacturer of excisable goods is required to obtain a license before commencement of production. The Central Excise Department exercises control over the manufacture and clearance of goods on payment of excise duty mainly in two ways. Certain goods like manufactured tobacco and matches are subject to physical control under which the goods are removed from the factory under the physical supervision of a Central Excise Officer on payment of duty assessed by him. Most of the goods are, however, under an alternative system of control called the Self Removal Procedure.


141 Rule 74.
Under this system the manufacturer has to get the rate of duty approved by the Department. Thereafter, he can assess the duty and remove the goods from the factory after payment of duty on his own. The manufacturer keeps an account current in which he makes credits from time to time and debits the duty determined at the time of removal of goods. The Central Excise Department exercise control through returns and documents submitted by the manufacturer supplemented by periodical local checks.

Duties of Customs

A. Customs tariff: Customs duties are levied under the Customs Act, 1962 and the Customs Tariff Act, 1975. India is a member of the General Agreement on Tariffs and Trade. Except for a few provisions relating to certain preferential areas and countries (e.g. UK, UAR, Yugoslavia), the customs duties are also neutral between Indian and foreign companies. A list of goods subject to import duty and the rates of duty are given in the First Schedule to the Customs Tariff Act which is commonly

\[\text{Secs. 4 & 5 of the Customs Tariff Act, 1975.}\]
known as the Import Tariff. Similarly, a list of goods subject to export duty and the rates of duty are given in the Second Schedule to that Act known as the Export Tariff. The classification of goods in the Tariff is based on the Brussels Tariff Nomenclature.

The rates of duty are specific in some cases and ad valorem in others. Since the Central Government have powers of exemption in respect of import duties and emergency powers of imposition and enhancement in the case of export duties, the effective rates of duty are regulated from time to time by executive notifications.

B. Additional and Auxiliary Duties: In the case of import goods, in addition to the basic import duties the following duties are also levied:

a. An additional duty known as countervailing duty is levied under Section 3 of the Customs Tariff Act. This duty is equivalent to the excise duty for the time being leviable on like goods

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143 Section 25 of the Customs Act and Section 8 of the Customs Tariff Act.
produced or manufactured in India.

b. An auxiliary duty of customs is levied under the Annual Finance Act. The rate in the Finance Act, 1983 is 50 per cent of the value of the goods. 144

C. **Assessable Value**: For purposes of **ad valorem** duties, the Central Government have powers to fix tariff values for any class of import or export goods. Where no tariff values are fixed, the value for levy of duty is the price at which like goods are ordinarily sold at the time and place of importation or exportation in the course of international trade where the seller and the buyer have no interest in the business of each other and the price is the sole consideration for the sale. 145

The material date for determination of the rate of duty and tariff value, if any, is the date of presentation of bill of entry to the proper Customs Officer or the date of entry inwards of

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144 Sec. 44 of the Finance Act, 1983.

145 Sec. 14 of the Customs Act, 1962.
the vessel whichever is later in the case of import goods. The export goods the material date is the date of presentation of shipping bill or bill of export or the date of entry outwards of the vessel whichever is later. 146

D. Export Promotion Measures: The following concessions are given in the interest of export promotion:

1. Duty Exemption Scheme: Under this Scheme raw materials imported for use in the manufacture of goods for executing specific export orders or in the manufacture of intermediate products for export or for supply to industrial units in Free Trade Zones or to hundred per cent Export Oriented Units are exempted from import duties. 147

Registered exporters are also allowed to import raw materials duty free against raw licences issued on the export of specified products. 148

146 Sections 15 and 16 ibid.


148 Appendix 29 ibid.
2. Hundred Per Cent Export Oriented Units: Industrial Units approved as hundred per cent Export Oriented Units are allowed duty free import of capital goods, components and raw materials. At the close of the period of export, however, duty has to be paid on capital goods on their depreciated value at the rate of duty in force at the time of import and on raw materials and components on their value at the time of import at the rates of duty in force at the time of clearance. 149

3. Free Trade Zones: Industrial Units in the Kandla Free Trade Zone and the Santa Cruz Electronics Export Processing Zone are allowed duty free import of capital goods components, raw materials etc., in connection with the production and packaging of goods for export. 150

4. Drawback: Drawback of customs duties paid is also admissible in the event of re-export of duty paid goods. Where the imported goods are identifiable as such at the time of re-export drawback

149 Appendix 33 ibid.

to the extent of 98 per cent of the duty paid could be allowed.\(^{151}\) In the case of manufactured goods, however, drawback in respect of duties paid on imported input is allowed at rates laid down under the Customs and Central Excise Duty Drawback Rules 1971. The rates of drawback are fixed either for certain manufactured goods on an All-Industry basis or in the form of specific brand rates for particular manufacturers.

**E. Appellate Procedure:** Both for excise and customs, judicial remedies are available to an aggrieved tax-payer analogous to those set out under income-tax.\(^{152}\)

**Sales Tax**

**A. General:** Sales-tax is the most important tax in the State List of taxes. The tax base is the turnover made up of the actual sale or purchase prices of goods. ‘Goods’ for purposes of this tax means tangible and moveable property only. The responsibility for the payment of tax rests on the

\(^{151}\) Sec. 74 ibid.

\(^{152}\) Chapter XV ibid and Chapter VIA of the Central Excises and Salt Act, 1944.
dealer though the burden may ultimately be shifted to the consumer.

The Constitution of India gives exclusive powers to each state to levy taxes on the sale or purchase of goods (except newspapers) taking place within that state\textsuperscript{153} subject however, to such conditions and restrictions as Parliament may impose in respect of goods declared to be of special importance in inter-state trade or commerce.\textsuperscript{154} The power to tax sale or purchase of goods in the course of inter-state trade or commerce is given to the Union\textsuperscript{155} though the proceeds thereof are also to be assigned and distributed to the states in which they are levied.\textsuperscript{156}

B. Import and Export Sales: A sale or purchase of

\textsuperscript{153}A sale or purchase takes place within a state where-

(i) In the case of specific or ascertained goods the goods are located in that state at the time when the contract of sale is made; and

(ii) in the case of unascertained or future goods the goods are located in that state at the time when they are appropriated to the contract by either party with the consent of the other. (Sec. 4 of the Central Sales Tax Act, 1956).

\textsuperscript{154}Article 286 (3) of the Constitution and Entry 54 of the State List.

\textsuperscript{155}Entry 9 2A of the Union List.

\textsuperscript{156}Article 269 of the Constitution.
goods in the course of import or export is exempt from tax. A sale or purchase is said to take place in the course of import or export if the said sale or purchase either occasions such import or export or is effected by transfer of documents of title to the goods while the goods are outside the customs frontier of India. It includes the last sale or purchase preceding the sale or purchase occasioning the export if such last sale or purchase took place after the foreign buyer's contract with a canalising agency or export house and for the purpose of meeting such contract.

C- Inter-State Sales: Tax on the sale or purchase of goods in the course of inter-state trade or commerce is levied under the Central Sales Tax Act, 1956. The general rate of tax is four per cent.

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157 Section 5 of the Central Sales Tax Act, 1956 and Consolidated Coffee Ltd. v. Coffee Board, Bangalore, 46 STC 164.

158 Article 286 ibid. of the Constitution of India.
A sale or purchase of goods is said to take place in the course of inter-state trade or commerce if such sale or purchase occasions the movement of goods from one state to another or is effected by a transfer of documents of title during the movement of goods from one state to another.\textsuperscript{159} The tax is collected and retained by the state in which the movement of goods in inter-state trade or commerce commences.\textsuperscript{160}

The Central Sales Tax Act also gives a list of goods declared to be of special importance in inter-state trade or commerce.\textsuperscript{161} The Act restricts taxes on the sale or purchase of these goods to a single point levy and requires that any tax paid on a sale or purchase of any of these goods in a state should be refunded if the goods are subsequently sold in the course of inter-state trade or commerce.\textsuperscript{162}

\textbf{D-Inter-State Sale:} Tax on sales or purchases of goods within each state is levied under various

\textsuperscript{159}Sec. 3 of the Central Sales Tax Act, 1956.
\textsuperscript{160}Sec. 9 (1) ibid.
\textsuperscript{161}Sec. 14 ibid.
\textsuperscript{162}Sec. 15 ibid.
State Sales Tax Acts. The taxes levied under different Acts vary in their incidence and operation. The rates of tax, generally, range between 1 and 15 per cent. The rates are high where the tax is a single point tax, i.e. where it is levied at only one point between production of goods and their sale to consumers. The rates are relatively low where the tax is multipoint, i.e., where it is levied on every sale between production of goods and their sale to the ultimate consumer. The basic necessities of life such as food, medicines and matches are, generally, exempt.

PAKISTAN

Income Tax

A - General: Income-tax, Super-tax and Surcharge are levied in Pakistan under the Income Tax Ordinance, 1979 and the Income Tax Rules, 1982 made there-under. The Act is administered by the Central Board of Revenue constituted under the Central Board of Revenue Act, 1924. The Ordinance, like the Indian Income-tax Act, 1961, is based on the old Indian Income Tax Act, 1922 and most of the concepts are common to the two countries.
Under the Ordinance, the assessment year commences on the first day of July and the preceding income year is either the financial year or, at the option of a business assessee whose accounts are made up on calendar year basis, the preceding calendar year. Income includes capital gains but capital gains attributable to depreciable business assets or immovable property are not taxed. In the case of a shareholder of a domestic company income does not include the face value of any bonus shares or the amount of any bonus issued by the company; for a Pakistani company such bonus or bonus shares are deemed to be income of the company for the particular year. Where a loan carries interest at a rate lower than the bank rate plus two per cent the difference is treated as income of the borrower. The rates of taxes are given in a Schedule to the Ordinance. The return of income has to be filed by 1 August or within 6 months and 15 days of the end of the

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163 Sec. 2 of the Ordinance.
164 Sec. 27. Capital gains from immovable property are taxed by provincial governments at rates varying from 5 to 20 per cent.
165 Sec. 12 ibid.
account year if that is later. 166 A taxpayer whose total income is not less than Rs. 50,000 has to file along with his return of income a wealth statement giving particulars of his total assets and liabilities. 167 The Income Tax Officer has to complete the assessment within two years of the end of the assessment year. 168

Tax has to be withheld at source and paid to government in respect of salaries, interest on securities and payments to non-residents. 169 In other cases where the total income is not less than Rs. 25,000 for a company or Rs. 50,000 in other cases, tax has to be paid in advance in four equal instalments on the 15th day of September, December, March and June. 170 In the following cases advance tax has to be withheld at source and paid to government.

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166 Sec. 55 ibid.
167 Sec. 58 ibid.
168 Sec 64 ibid.
169 Sec. 50 ibid.
170 Sec. 53 ibid.
a. Any person, other than a Pakistani private company with a paid-up capital of less than Rs. 3 million, making any payment under a contract with government or a local authority or a company or a foreign contractor, consultant or consortium, has to withhold advance tax at the rate of 3 per cent of such payment if the amount of the payment exceeds in any year Rs. 50,000 in the case of a works or supply contract and Rs. 10,000 in the case of a service contract.

b. The Collector of Customs has to withhold advance tax at the rate of 1 1/2 per cent in the case of assesses liable to pay advance tax and 2 percent in other cases of the value (including customs duty and sales-tax) of imported goods.

c. The person collecting motor vehicles tax has to withhold advance tax at rates which are related to the carrying capacity of goods and passenger transport vehicles.

d. Any auctioneer selling property belonging to government, local authorities, public companies, foreign companies or foreign contractors, consultants
or consortia has to withhold advance tax at 3 per cent of the sale price. The balance of tax, if any, has to be paid along with the return of income. Any further tax demanded on completion of assessment by the Income-tax Officer has to be paid within such time as may be specified in the notice of demand. A default in making any of these payments of tax in the manner prescribed would invite, apart from other penal consequences, a liability to pay additional tax at the rate of 24 per cent per annum in respect of advance tax and 15 per cent per annum in respect of withheld taxes and taxes payable with return or on demand. A persistent default would invite coercive recovery proceedings.

B-Company. The terms 'Pakistani company', 'domestic company' and 'foreign company' are defined on the same lines as in the Indian Act. The Ordinance further includes a definition of 'public company' as a company in which not less than 50 per cent of the shares are held by government or whose shares are listed in a registered stock exchange in Pakistan. This definition is important because public companies are entitled

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171 Sec. 50 read with the First and Second Schedules ibid.
172 Sec. 54 ibid.
173 Sec. 85 ibid.
174 Sec. 86 to 95 ibid.
to certain tax benefits. 175

C-Residence and Tax Liability: The residential status of a company as well as the extent of tax liability of resident and non-resident persons are on the same lines as in the Indian Act. 176

D-Computation of Business Income: The principles of computation of business income are also the same as in the Indian Act. The following expenses are specifically disallowed.

a. Any cess, rate or tax on profits or gains of business.

b. Any payments to a non-resident person if tax thereon has not been withheld and paid.

c. Any payments on account of salaries if tax thereon has not been withheld and paid.

d. Any expenditure in the nature of head office expenditure in so far as it exceeds the lower of the expenditure attributable to the business in Pakistan or the annual average of such expenditure in the earlier three years. 177

E- Rates of Tax on Companies: The rates of tax are as under:

I- Income-tax

On income excluding income from dividends, bonus or bonus shares - 30 per cent

175 Sec. 2 read with the First Schedule ibid.
176 Sec. 2 and 11 ibid.
177 Sec. 24 read with Rule 20.
II - Super-tax

On income excluding income from dividends, bonus or bonus shares:

- Banking companies - 35 per cent
- Others - 25 per cent

On dividend income

- 5 per cent if the recipient is a public company.
- 15 per cent if the recipient is a foreign company.
- 20 per cent in other cases.

On bonus - issued by the company

- Public companies - 10 per cent
- Others - 15 per cent

III - Surcharge:

5 per cent of income-tax and super-tax

These rates are subject to the following rebates/reductions:

a. Capital gains in respect of assets held for over 12 months are taxed only at 25 per cent.

b. Income from technical fees earned abroad by non-resident companies and repatriated
to Pakistan is given a rebate of 30 per cent of income-tax and super-tax.

c. Income from construction works earned abroad by Pakistani companies and repatriated to Pakistan is given full rebate of super-tax.

d. Profits of domestic companies from export sales of goods (other than raw cotton and other notified goods) manufactured in Pakistan are given a rebate of 55 per cent of income-tax and super-tax. Other foreign earnings of such companies are given a rebate of 15 per cent of super-tax.

e. Domestic companies are given rebates of super-tax ranging from 5 to 15 per cent depending on capital investment and the nature of business. 178

P- Tax Incentives: The following are some of the more important tax incentives:

1. Depreciation

The provisions for normal depreciation, extra shift allowance and balancing allowances/charge are

178 Parts II and IV of the First Schedule to the Ordinance.
similar to those in the Indian Act. The general rates of depreciation are 5 to 10 per cent for buildings, 10 per cent for plant and machinery and 20 per cent for motor vehicles. Over and above these allowances, initial depreciation is allowed in the first year in respect of new buildings, plant or machinery erected or installed between July, 1976 and June, 1983, at the rate of 25 per cent for residential buildings for industrial labour, 10 per cent for other buildings, 40 per cent for plant and machinery and 30 per cent for ships. The aggregate of all allowances for depreciation should not exceed the original cost of the asset.

There is no provision for unabsorbed depreciation allowance being separately carried forward for set off in future years. 179

In the case of a business of exploration and extraction of petroleum or other mineral deposits, depletion allowance is given at the rate of 15 per cent of gross receipts, subject to a maximum of 50 per cent of the profits of the year, in the case of petroleum and 15 per cent of

179 Third Schedule to the Ordinance.
of the total income or 50 per cent of the capital employed, whichever is less, in the case of other minerals. Exploration expenses incurred before the commencement of commercial production are also allowed to be charged off over a period of 10 years after the commencement of such production. 180

2. New Investment

New investment by Pakistani companies in the purchase of plant and machinery between July 1976 and June 1983 for purposes of replacement, balancing or modernisation, is given a tax credit at the rate of 50 per cent of such new investment. The unabsorbed amount of the tax credit can be carried forward up to two succeeding assessment years. 181

Approved industrial undertakings set up by Pakistani companies in specified areas of the country during July 1975 to June 1983 are given a tax exemption to the extent of 10 per cent of the capital employed in the year of commencement of commercial production as well as in four subsequent years going not beyond June 1985. 182

180 Fifth Schedule to the Ordinance.
181 Sec. 107 ibid.
182 Sec. 48 ibid.
Companies investing in shares of Pakistani public companies setting up approved industrial undertakings in specified areas are also given tax credit at 15 to 30 per cent (depending on the area of location) of investment provided the shares are not transferred or otherwise disposed of within 5 years. This tax credit can be carried forward without any time limit.\textsuperscript{183}

3. Tax Holiday

Pakistani companies setting up industrial undertakings in specified areas of the country (presently, before 30 June, 1983) are entitled to a full tax holiday for a period of 5 years.\textsuperscript{184}

Pakistani companies setting up, between July 1981 and June 1985, undertakings engaged in the exploration and extraction of specified minerals are entitled to a full tax holiday for 5 years followed by a partial tax holiday of 50 per cent for another 5 years.\textsuperscript{185}

Industrial undertakings set up in an Export Processing Zone\textsuperscript{186} are entitled to a full tax holiday.

\textsuperscript{183}Sec. 106 ibid.

\textsuperscript{184}Clauses 119-122 and 124 of the Second Schedule to the Ordinance.

\textsuperscript{185}Clause 123 of the Second Schedule read with Part II (1) thereof.

\textsuperscript{186}An Export Processing Zone is being set up in Karachi.
day for 5 years followed by a partial tax holiday of 75 per cent for another 5 years. Foreign profits of such undertakings arising from approved activities are totally exempt.\(^{187}\)

4. **Expenditure on Scientific research**

Capital as well as revenue expenditure on scientific research related to the business carried on by the taxpayer and any sums contributed to a scientific research institution for such research are allowed to be deducted in full in the computation of business income.\(^{188}\)

5. **Education and Training**

Capital as well as revenue expenditure on educational institutions or hospitals for employees or their families or recognized training institutes for industrial workers are also allowed to be deducted in full in the computation of business income.\(^{189}\)

6. **Export Publicity**

Domestic companies are allowed a weighted deduction of \(1 \frac{1}{3}\) times the amount of expenditure

\(^{187}\)Clauses 126 and 128 of the Second Schedule read with Part II (2) thereof.

\(^{188}\)Sec. 23 ibid.

\(^{189}\)Sec. 23 ibid.
incurred on advertisement, publicity or provision of samples, outside Pakistan, in connection with the export sales of specified goods.\textsuperscript{190}

7. \textbf{Technical Fees}

Income by way of technical fees earned abroad under an approved agreement and brought into Pakistan is fully exempt.\textsuperscript{191}

8. \textbf{Carry-forward of losses}

Business losses can be carried forward for set off against future years' profits of the same business up to six succeeding assessment years. In the case of industries in Export Processing Zone such losses can be carried forward indefinitely. Losses of wholly-owned subsidiaries can be set off against profits of holding companies and also carried forward for two succeeding assessment years for such set off.\textsuperscript{192}

\begin{itemize}
\item \textbf{G - International Aspects}: The following are some of the provisions of special interest to foreign investors.
\end{itemize}

\textsuperscript{190} Proviso to Sec. 23 (1) ibid.
\textsuperscript{191} Clause 139 of the Second Schedule to the Ordinance.
\textsuperscript{192} Sec. 34A and 35 ibid.
1. **Taxation at Source**

The Ordinance contains provisions analogous to those of the Indian Income Tax Act in respect of incomes of non-residents from property, dividends, business connection, interest, royalty and technical fees being deemed to accrue or arise in Pakistan. Such incomes are then included in the total income of the non-resident and taxed at the rates already mentioned.\(^{193}\)

2. **Foreign Shipping Lines**

In the case of a non-resident ship owner or charterer, tax is levied at the rate of 8 per cent on the aggregate of payments wherever received on account of the carriage of passengers, live-stock, mail or goods shipped at a Pakistani port, and payments received in Pakistan on account of the carriage of the said things shipped at any port outside Pakistan.\(^{194}\)

3. **Foreign Airlines**

In the case of non-resident owners or charterers of aircraft, tax is levied at the rate

\(^{193}\)Sec. 12 ibid.

\(^{194}\)Sec. 80 ibid.
of 3 per cent on the aggregate of payments wherever received in respect of carriage of passengers, mail, livestock or goods loaded at an airport in Pakistan, and payment received in Pakistan on account of the carriage of the said things loaded at any airport outside Pakistan.

4. **Non-resident Partner, Statutory Agent, and Diversion of Income to Non-resident.**

The Ordinance contains provisions on these matters, similar to those in the Indian Act.

5. **Special Exemptions**

The following are some of the exemptions of special interest to non-residents:

a. **Foreign Technicians**: In the case of a foreign technician employed in a new industrial undertaking on an approved contract either before the commencement of commercial production or during the first five years after the commencement of such production the salary income is exempt from tax.

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195 Sec. 50A ibid.

196 Sec. 69, 78, 79 ibid.
On expiry of the exemption period tax paid by the employer on such salary income is exempt for a further period of five years.\textsuperscript{197}

b. Salary incomes of foreigners employed in industrial undertakings in Export Processing Zone are exempt for a period of 5 years.\textsuperscript{198}

c. \textbf{Interest Income} : Interest income of a non-resident in respect of a private loan for an approved project in Pakistan or on monies borrowed under the approved loan agreement is exempt from tax.

Interest received by a non-resident from an industrial undertaking in Pakistan on monies borrowed or debts incurred abroad for purchase of capital plant and machinery is exempt from so much of the tax as exceeds the tax paid on such interest in the foreign country.\textsuperscript{199}

7. \textbf{Tax Treaties and Unilateral Tax Relief}

The Ordinance contains provisions analogous

\textsuperscript{197} \textit{Clauses 7 and 8 of the Second Schedule.}

\textsuperscript{198} \textit{Clause 127 ibid.}

\textsuperscript{199} \textit{Clauses 75, 76 and 77 ibid.}
to those of the Indian Act on these matters. 200
Pakistan has tax treaties with Austria, Bangladesh, Belgium, Canada, Denmark, France, Germany, Ireland, Japan, Libya, Malta, Poland, Romania, Sri Lanka, Sweden, Switzerland, Thailand, U.K. and U.S. Tax treaties with many other countries are being negotiated. 201 The treaties usually exempt royalties, technical fees and in some cases interest, where the recipient has a permanent establishment in Pakistan. These also provide for lesser rates of dividend tax. 202

H - Reassessment, Prosecution and Appeals: A completed assessment can be reopened within ten years from the end of the assessment year if there is definite information that any income has escaped assessment or has been under-assessed. 203

200 Sec. 163, 164 of the Ordinance.
203 Sec. 65 ibid.
A default in complying with the provisions of the Ordinance may involve the taxpayer not only in penal consequences but also prosecution.\textsuperscript{204} An aggrieved taxpayer has appellate and judicial remedies available to him on the same lines as under the Indian Act.\textsuperscript{205}

**Duties of Customs**

Customs duties are levied under the Customs Act 1969. The classification of commodities is based on the Brussels Tariff Nomenclature. The rates of duty are mainly ad valorem ranging between 0 and 125 per cent. The assessable value is the 'normal price', \textit{i.e.}, the price that the goods would fetch on the date of import on a sale in the open market between a buyer and a seller, independent of each other.\textsuperscript{206}

The federal government has general powers of exemption while the Central Board of Revenue has such powers in individual cases of exceptional nature.\textsuperscript{207}

\textsuperscript{204}Chapters XI and XII ibid.
\textsuperscript{205}Chapter XIII ibid.
\textsuperscript{206}Sec. 25 and 30 of the Customs Act, 1969.
\textsuperscript{207}Sec. 19 and 20 ibid.
If identifiable duty-paid goods are re-exported within two years, 7/8th of the duty paid is repaid as draw-back. Draw-back is also allowed in the case of export of manufactured goods containing duty-paid imported inputs.208

Import of machinery and equipment required for exploration and drilling for oil is allowed free of customs duty. Also contractors and sub-contractors of oil companies can import equipment in their own names at a concessional rate of duty of 5 1/4 per cent and store such equipment to meet the needs of various oil companies.209 Imports and exports in Export Processing Zone are free of export and import duties. Export oriented units are allowed duty-free import of machinery upto Rs. 2.5 million for balancing, modernisation and replacement.210

An aggrieved taxpayers can file an appeal to a superior departmental authority. He may also approach the Central Board of Revenue or the federal government in revision.211

208 Sec. 35 to 37 ibid.
211 Chapter XIX of the Customs Act, 1969.
Duties of Excise

Duties of excise are levied under the Central Excises and Salt Act, 1944, the main provisions of which have already been described in the Indian section. The tariff schedule in Pakistan was completely revised in 1979 on the lines of the Customs tariff based on the Brussels Tariff Nomenclature. The Schedule is confined to specified goods; it does not contain a residual item of the type added in the Indian tariff. The Finance Ordinance, 1970, extended the levy of excise duty from 'goods' to 'services, facilities and utilities'. A list of excisable services is also given in the tariff schedule.

The Act also empowers the federal government to levy, by notification, regulatory duties of excise in addition to excise duties on excisable as well as non excisable goods and services.

Sales Tax

A single point sales tax at a standard rate of 12.5 per cent is levied under the Sales Tax Act, 1951.

\(^{212}\)Sec. 2 (dd) of the Central Excise and Salt Act, 1944.

\(^{213}\)Sec. 3A ibid.
The tax is on the value of all goods produced or manufactured in Pakistan, payable by the manufacturer or producer, all goods imported into Pakistan, payable by the importer, and all goods sold by a licensed wholesaler, payable by the licensed wholesaler. The value is the sale price or in the case of imported goods the duty paid value of such goods.\(^{214}\)

The federal government have powers, under the Act, to levy an additional regulatory tax at a maximum rate of 15 per cent on notified goods.\(^{215}\)

The tax has to be paid monthly and a return is to be filed quarterly. Failure to pay tax invites, apart from other penal consequences, liability to pay additional tax at the rate of 15 per cent per annum, of the amount of tax due.\(^{216}\)

If imported goods on which tax has been paid on importation are re-exported within two years seven-eighth of the tax is repaid as draw-back.\(^{217}\)

\(^{214}\)Sec. 3 of the the Sales Tax Act, 1951.

\(^{215}\)Sec. 3A ibid.

\(^{216}\)Sec. 10, 12, 12A ibid.

\(^{217}\)Sec. 27C ibid.
Income Tax
A- General : Income tax is levied under the Inland Revenue Act (No. 28) of 1979 which replaced the Inland Revenue Act (No. 4) of 1963 with effect from 1 April, 1979. The Act is administered by the Commissioner General of Inland Revenue appointed under section 157 thereof. Income tax is charged in respect of the profits and income of every person for every assessment year commencing on 1 April at the rates specified in the schedules to the Act. Profits and income include profits from trade, business or profession 'for however short a period carried on or exercised'. These also include capital gains.218 Every taxpayer is under an obligation to file a return of his income with an Assessor by 30 November following.219 The Assessor has to complete the assessment within three years of the end of the assessment year.220 The tax has to be paid in advance on the basis of a self-assessment in four equal instalments on the 15th day of August, November, November, November, November.

218 Sec. 2 and 3 of the Inland Revenue Act, 1979.
219 Sec. 92 ibid.
220 Sec. 115 ibid.
February and May.\textsuperscript{221} Any further tax found due on completion of assessment by the Assessor is required to be paid within such time as may be indicated in the notice of assessment.\textsuperscript{222} For certain incomes like salaries, dividends of resident companies other than quoted public companies and interest payments made to non-residents, tax has to be deducted at source and paid to government.\textsuperscript{223}

\textbf{B - Company:} A company is a taxable person. The Act defines a company to mean any company incorporated or registered under any law in force in Sri Lanka or elsewhere, including a public corporation.\textsuperscript{224} Resident companies are divided into three categories, peoples' companies, small companies and other companies. A people's company is a company which satisfies the following conditions:

- It is not a private company
- It has over 100 shareholders
- The nominal value of each of its shares does not exceed \textcurrency{Rs.} 10.
- Its shares are freely transferable.

\textsuperscript{221} Sec. 97 ibid.
\textsuperscript{222} Sec. 125 ibid.
\textsuperscript{223} Sec. 98, 37, 81 ibid.
\textsuperscript{224} Sec. 163 ibid.
- More than 5 per cent of its shares are not held (directly or indirectly) by one person individually or together with his wife or minor children.

- There are three or more directors each owning one or more shares

- None of its directors holds office as director of another people's company

- No other company holds any of its shares directly or indirectly.

A small company is a company whose issued capital does not exceed Rs. 500,000 and which has neither reduced its capital nor been reconstituted on or after 15 November, 1978.225

A company pays tax on its profits as well as on the dividends distributed out of these profits; it is entitled to withhold tax from dividends for which the shareholders get credit in their individual assessments.226 A non-resident company pays tax on its profits and also on its remittances abroad but not on dividends distributed in Sri Lanka.227

C- Residence and tax liability: The extent of tax liability depends on the factum of residence in Sri

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225 Sec. 33 ibid.

226 Quoted public companies do not pay tax on dividends.

227 Sec. 34 ibid.
Lanka. An individual is resident if he is in Sri Lanka for at least six months. A company is resident if it has its registered or principal office in Sri Lanka or the control and management of its business is exercised in Sri Lanka. 228 The tax liability of a resident person extends to all profits and income 'wherever arising'; the tax liability of a non-resident person is confined to profits and income 'arising in or derived from Sri Lanka' 229

D- Computation of business income: The profits and income from business are computed according to ordinary commercial principles after allowing deductions for expenses including depreciation. The Act spells out certain expenses which include any expenditure on scientific, industrial or agricultural research for the development of the trade or business carried on by the taxpayer and then goes on to lay down a general principle that any expenditure 'not being money expended for the purpose of producing such profits or income' will not be allowed. The following

228 Sec. 67 ibid.
229 Sec. 2 ibid.
expenses are specifically disallowed:

1. Expenditure on vehicles used partly for private purposes by the employees or on travel of employees between residence and place of work.
2. Expenditure on travel abroad otherwise than in connection with exports or export promotion.
3. Expenditure on entertainment or entertainment allowances.
4. One-fourth of advertisement expenditure other than that relating to export trade or export promotion.
5. Contributions to unapproved pension or provident funds.
6. Payment on account of income tax.

E- Rates of tax: The rates of tax applicable from the assessment year 1980-81 are:

I. Resident companies

<table>
<thead>
<tr>
<th>Category</th>
<th>Rate of Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>Peoples' company</td>
<td>40 per cent</td>
</tr>
<tr>
<td>Small Company</td>
<td></td>
</tr>
<tr>
<td>On the first Rs. 50,000</td>
<td>20 per cent</td>
</tr>
<tr>
<td>On the next Rs. 1,00,000</td>
<td>30 per cent</td>
</tr>
<tr>
<td>On the balance</td>
<td>40 per cent</td>
</tr>
<tr>
<td>Other company</td>
<td>50 per cent</td>
</tr>
</tbody>
</table>

Plus, in every case$, 20 per cent of gross dividends distributed out of the year's profits.

\[230\] Sec. 23 and 24 ibid.

\[231\] A quoted public company, i.e. a resident company whose shares are quoted in any official list published by the Colombo Broker's Association, or similar other body approved by the Minister, pays tax at 40 per cent without any tax on dividends (sec. 167 and 33 ibid).
II. Non-resident companies - 50 per cent

Plus 5 per cent of taxable income,

Plus, 33 1/3 per cent of aggregated remittances abroad, if such aggregate is less than 1/3rd of taxable income, and 11 1/9 per cent of taxable income if such aggregate is not less than 1/3rd of the taxable income. 232

A company which is controlled by not more than five persons and which has not distributed to its shareholders a reasonable part of its profits for any year of assessment is taxed at the highest individual rate of tax (which is 55 per cent) on its retained profits in addition to the corporation tax. 233

Capital gains are taxed at a lower rate of 25 per cent. Where a capital gain arises from change of ownership of property, 25 per cent or 50 per cent of such capital gain, depending upon whether the property has been held for over five but not over fifteen years or for over fifteen years respectively, is exempt from tax. 234

**Tax Incentives:** The following are some of the more important tax incentives:

232 'Remittances' do not include income by way of dividends from resident companies if tax has been withheld therefrom or if the dividends are tax free. 'Remittances' also do not include sale proceeds or profits made and retained abroad. (Sec. 34 ibid).

233 Sec. 39 ibid.

234 Sec. 7 and 32 ibid.
1. **Foreign Currency Units**

Incomes of foreign currency banking units from all off-shore transactions and from such on-shore transactions as are approved by the Minister having regard to the foreign exchange benefits likely to accrue to the country are exempt.\textsuperscript{235}

2. **GCEC Undertakings**

Undertakings set up in the Free Trade Zone under agreement with the Greater Colombo Economic Commission are controlled by the taxation provisions of such agreement which over-ride the Act. The agreements provide for 100 per cent tax exemption for corporate and personal incomes, royalties and dividends for periods ranging from 7 to 10 years depending on factors like capital investment, foreign exchange earnings, and employment created. After this initial tax holiday period there is concessionary tax for another 15 years comprising a tax based on turnover of 2 to 5 per cent in place of the normal income and corporate tax.\textsuperscript{236}

\textsuperscript{235}Sec. 8 ibid.

\textsuperscript{236}Indian Institute of Foreign Trade, *Foreign Trade Review*, vol. 16 (Jan-March 1982) p. 351.
3. **New Quoted Companies**

Undertakings carried on by new public companies approved by the Minister are entitled to a 5-year tax holiday.\(^{237}\)

4. **Tourist Hotels**

A new undertaking operating a tourist hotel is entitled to 10 years' tax holiday if it is run by a quoted public company with subscribed equity capital of not less than Rs. 100 million and approved by the Minister on the recommendation of the Ceylon Tourist Board. Existing hotels, earlier eligible for a five year tax holiday, are also entitled to full exemption of tax for 5 years in respect of profits from additional rooms constructed on or after 15 November, 1979.\(^{238}\)

5. **Property Development**

Quoted public companies engaged in approved property development projects are entitled to a ten year tax holiday.\(^{239}\)

\(^{237}\) Sec. 22C ibid.

\(^{238}\) Sec. 16, 16A, 16B ibid.

\(^{239}\) Sec. 228 ibid.
6. Non-Traditional Plants

Quoted public companies with a paid up capital of not less than 100 million rupees and approved by the Minister, engaged in the cultivation of plants other than tea, rubber, coconut or paddy or in processing them are entitled to a ten year tax holiday. 240

7. Contract Incomes

Incomes from approved contracts with Mahaweli Authority of Sri Lanka of quoted public companies engaged solely in such contracts are exempt for a period of 5 years.241

8. Export Profits

Export profits of non-traditional exports of new undertakings approved by the Minister are exempt for a period of 5 years.242

In respect of old undertakings (set up prior to 1 April, 1972), a tax exemption for five years is available for so much of the export profits as are in

240 Sec. 22D inserted by the Inland Revenue (Amendment) Act No. 40 of 1981.

241 Sec. 22A ibid.

242 Exports other than those of traditional commodities like tea, rubber, coconut oil, copra, See Sec. 20 ibid.
excess of the average of export profits of the preceding three years. 243

9. Capital Gains

Capital gains relating to the shares of GOBC enterprises or quoted public companies are exempt from tax. 244

10. Dividends

All dividends declared out of tax exempted profits (GOBC undertakings, tourist hotels, etc.) are exempt in the hands of the shareholders for the period of the tax holiday and within one year thereafter. 245

11. Approved Investments

Sums invested in equity shares of approved undertakings, such as GOBC undertakings, Export undertakings, Land and Housing Development undertakings, or any undertakings considered essential for the economic progress of the country are deducted in the computation of income upto one-third of the assessable income along with certain other donations to charities. 246

243 Section 20 as amended by the Inland Revenue (Amendment) Act No. 40 of 1981.
244 Sec. 14 ibid.
245 Sec. 11 ibid.
246 Sec. 31 ibid.
12. **Carry Forward of Losses**

Losses of business or profession are allowed to be carried forward for set off in future years. Capital losses are allowed to be carried forward for set off against future capital losses.\(^{247}\)

**International Aspects**: The following are some of the provisions of special interest to foreign investors:

1. **Assessment on Agent**

   A non-resident person is assessable either directly or in the name of his agent, whether such agent is in receipt of the profits or income or not.\(^{248}\)

2. **Source of income**

   Profits and income arising in or derived from Sri Lanka include:

   a. All profits or income derived from business, transacted in Sri Lanka, whether directly or through an agent.\(^{249}\)

   b. Interest payable to a non-resident person on a loan if the interest is borne, directly or indirectly, by a resident person or the loan is brought to or used in Sri Lanka.\(^{250}\)

   c. Royalty payable to a non-resident person if it is borne, directly or indirectly, by a resident person or is allowable as a business

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\(^{247}\)Sec. 29 ibid.

\(^{248}\)Sec. 68 ibid.

\(^{249}\)Sec. 2 ibid.

\(^{250}\)Sec. 30A ibid.
loss in Sri Lanka.\textsuperscript{251}

d. Profits arising, from a person in Sri Lanka affecting an insurance (in Sri Lanka or outside) or selling a property (situated in Sri Lanka or to be brought into Sri Lanka) on behalf of a non-resident person, whether moneys are paid to or received by the non-resident person directly or otherwise. The person in Sri Lanka is assessed to tax as agent of such non-resident person.\textsuperscript{252}

3. Deemed Non-resident

A foreigner employed in Sri Lanka is deemed to be non-resident for a period of initial 3 years and taxed at a lower rate of 25\% only in respect of income arising in or derived from Sri Lanka.\textsuperscript{253}

4. Foreign Shipping

In the case of shipping profits of non-residents, 6 per cent of the sum receivable on account of the carrying of passengers, mails, livestock and goods shipped in Sri Lanka (other than goods brought to Sri Lanka solely for trans-shipment) is deemed to be profits arising in Sri Lanka.\textsuperscript{254}

\textsuperscript{251}Sec. 80B (Inserted by the Inland Revenue (Amendment) Act No. 40 of 1981.

\textsuperscript{252}Sec. 68

\textsuperscript{253}Sec. 67

\textsuperscript{254}Sec. 74 ibid.
5. **Non-resident Aircraft**

In the case of non-resident owners or charterers of aircraft, full profits arising from the carriage of passengers, mails, livestock or goods loaded into the aircraft in Sri Lanka are deemed to arise in Sri Lanka.\(^{255}\)

6. **Non-resident Partner**

The share of a non-resident partner in a partnership is assessable in the name of the partnership or of any resident partner or of any agent of the non-resident partner in Sri Lanka.\(^{256}\)

7. **Diversion of Income to Non-resident**

where there is a close connection between a non-resident person and a resident person and the business between them is so arranged as to produce less than the ordinary profits to the non-resident person, the business done by the non-resident person in pursuance of such connection is deemed to be carried on in Sri Lanka and the non-resident person is assessable in respect of his profits from such business.

\(^{255}\text{Sec. 77 ibid.}\)

\(^{256}\text{Sec. 65 ibid.}\)

\(^{257}\)
business in the name of the resident person as if the resident person were his agent. 257

8. **Tax Treaties**

Sri Lanka has entered into tax treaties for avoidance of double taxation with India, Pakistan, Sweden, Denmark, Norway, Federal Republic of Germany, Singapore, U.K., Japan, Malaysia, Czecho-slovakia, France, Poland, Bangladesh, Canada, Netherlands, Belgium, Switzerland, Italy, Finland and Romania. These treaties provide for concessional rates of tax at source of 15 per cent on dividends, 10 per cent on interest and 10 per cent on royalties. Most of them have tax sparing provisions. Under the Act, a tax treaty has to be approved by Parliament by a resolution and once it is so approved it has the force of law notwithstanding anything in any other written law. 258

9. **Special Exemptions**

The following incomes of non-residents are exempt:

257 Sec. 69 ibid.

258 Sec. 82 ibid.
a. Any income of a foreign scientist, technician, expert or adviser employed in government or a government or other approved enterprise or approved tourist hotel or GCEC undertaking, or in connection with a profit exempt contract. 259

b. Interest income of any foreign entity from a loan to Government or public corporation or government institution or commercial bank or any other undertaking, if such loan is approved by the Minister as being essential for the economic progress of Sri Lanka. 260

c. Any management fees, calculated as a percentage of gross profits and paid to a non-resident person by a company operating a tourist hotel during the tax holiday period if such payment is approved by the Minister on the recommendation of the Ceylon Tourist Board. 261

d. Profits of non-residents from contracts entered into with, Government, approved tourist hotels and approved public corporations and insti-
tutions where such contracts provide that the sums paid under them would not be liable to tax. 262

e. Royalty payments by GCSC undertakings to non-residents during the tax holiday period. 263

f. Any dividend paid to a non-resident by a GCSC undertaking. 264

II- Additional Assessment, Penalties, Prosecutions and Appeals: In a case of non-assessment or under-assessment 'due to fraud or wilful evasion' on the part of the taxpayer, assessment or additional assessment may be made at any time. 265

Failure to comply with the provisions of the Act would invite penalties or prosecution under the Act. 266 In the event of persistent default in payment of taxes recovery proceedings may be taken up. 267 An aggrieved taxpayer can file an appeal to the Commissioner General of Inland Revenue. A second appeal lies to an extra-departmental Board of Review appointed by the Minister. The decision

262 Sec. 22 ibid.
263 Sec. 15 (j) ibid.
264 Sec. 11 ibid.
265 Sec. 115 ibid.
266 Sec. 96, 125, 151 ibid.
267 Sec. 126 et. seq.
of the Board is final on facts. On questions of law a reference may be taken to the Court of Appeal.268

Wealth Tax

Wealth Tax is levied under Section 41 of the Inland Revenue Act, 1979 on the net wealth comprising the aggregate value of wealth minus the aggregate value of all debts on the first day of the assessment year. Immovable property situated outside Sri Lanka (for non-residents all properties situated outside Sri Lanka) is excluded. The rates of tax range from 1/2 per cent to 2 per cent. The tax is not charged in the case of companies but a non-resident company having immovable property in Sri Lanka has to pay wealth tax of 1 per cent in respect of such immovable property, its value being taken at five times the taxable income accruing from it. Where the aggregate of income-tax and wealth-tax exceeds 80 per cent of the taxable income wealth-tax is reduced to the extent of such excess.269

268Sec. 117-120 ibid.
269Sec. 41 - 48, 86 ibid.
Gift Tax

Gift tax is levied under Section 51 of the Inland Revenue Act, 1979 in respect of gifts made by all persons including companies. Gifts of immovable property situated outside Sri Lanka, gifts by non-resident foreigners of movable property situated outside Sri Lanka and gifts by companies to government, to local authorities or to approved charities are exempt. The rates of gift tax range from 5 to 70 per cent; the rate for companies being 50 per cent. 270

Estate Duty

Estate Duty is levied under the Estate Duty Act No. 13 of 1980. The duty is charged at progressive rates going upto 70 per cent on the value of the estate of a deceased person. The basis for liability is domicile and not residence or citizenship. In the case of a person domiciled in Sri Lanka the estate would include all property wherever situated, except immovable property situated outside Sri Lanka. In the case of a person not

270 Sec. 51 - 58 ibid.
domiciled in Sri Lanka only property situated in Sri Lanka is taken. 271 Where a foreigner, not domiciled in Sri Lanka, is a shareholder of a foreign company which holds property in Sri Lanka, there is no liability to duty. 272

Turnover Tax

Business turnover tax is levied under the Turnover Tax Act, No. 69 of 1981 on the turnover, (a) of a business carried on in Sri Lanka, (b) from services rendered outside Sri Lanka, for which payment is made from Sri Lanka, (c) on import into Sri Lanka of any manufactured article. 273 There is no liability on exports and imports by GOEC enterprises. The foreign investor is not liable to turnover tax on monies brought into Sri Lanka or on sale of shares. 274 The tax is payable every quarter. 275 In respect of turnover on imports the tax is collected

271 Sec. 78 of the Estate Duty Act.
273 Sec. 2, 5 of the Turnover Tax Act, 1981.
274 Ambalavaner, n. 272.
275 Sec. 2 ibid.
by the Principal Collector of Customs along with the customs duty. 276

Every manufacturer has to register himself with the Commissioner General. 277

Transfer of Property Tax

This tax is levied under the Finance Act No. 11 of 1963. Transfers of shares or immovable property situated in Sri Lanka to non-citizens are liable to tax at 100 per cent of the value of the property transferred. The first issue of shares in Sri Lanka by a company to a non-citizen is not, however, liable to this tax. Also transfers of shares to GCEC companies are free from this tax. Further, there is no liability for transfer to a Sri Lanka company even if all the shares are held by non-citizens. 274

Duty of Customs

Customs duties are levied under the Customs Ordinance administered by the Principal Collector

276 Sec. 12 ibid.
277 Sec. 46 ibid.
of Customs. The rates of duty are mostly ad valorem. There are five basic slabs of duty ranging from 5 to 100 per cent. Essential goods like raw materials not produced locally and machinery attracted the lowest rates and luxury items, the highest. 278

The tariff classification is based on the Brussels Tariff Nomenclature (BTN). The assessable value is normally the C.I.F. value. The agreements with GEC undertakings provide for exemption from all import and export duties. Approved export oriented companies are also entitled to a rebate on customs duty on imported raw materials at the point of export of finished products. 279

Sri Lanka is a member of the GATT.


In Bangladesh income tax and super tax are levied under the Income Tax Act, 1922, read with the Annual Finance Act of the year concerned. The Act is administered by the National Board of Revenue set up under the Board of Revenue Order, 1972. Since this Act is, as already mentioned, the basis of both the Indian and Pakistani laws on the subject, the main provisions, concepts and procedures are similar.

Tax is charged in every year commencing on 1 July in respect of the total income of the preceding year at the rates given in the Annual Finance Act. As in the case of Pakistan the income of a company includes the face value of any bonus shares or the amount of any bonus declared, issued or paid. In addition, in Bangladesh agricultural income is also subject to tax under the same Act. The provisions regarding payment

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Section 2 (6C) of the Income Tax Act, 1922.

Section 9A ibid.
of tax are analogous to those in Pakistan.282

B-Company: The Bangladesh law also gives a special definition of "Public company" as in Pakistan, as public companies are given concessional tax treatment.

C-Residence and Tax Liability: The provisions about the tax liability of resident and non-resident persons and the determination of residential status of a company are similar to those in India and Pakistan.

D-Computation of Business Income: The following expenses are not allowed to be deducted in the computation of business income:

a. Any cess, rate or tax on profits or gains of business,

b. Any payment on account of salary on which tax has not been deducted at source and paid to government,

c. Any brokerage or commission paid to a non-resident person in respect of which tax has not been deducted at source and paid to government,

d. Entertainment expenses in excess of certain prescribed limits,

e. Perquisites to employees in excess of 50

\[282\] Sections 18, 18A ibid.
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per cent of salary or 50,000 takas, whichever is less.\textsuperscript{283}

\textbf{Rates of Tax}: The following are the rates of taxes in respect of companies:

1. Income Tax - 30 per cent

2. Super Tax:
   - on income in excess of 1,50,000 takas - 25 per cent
   - on income from company dividends:
     - Public companies - 15 per cent
     - Others - 20 per cent
   - on bonus shares or bonus
     - Public companies - 15 per cent
     - Others - 20 per cent

Capital gains in respect of assets held for not more than one year are charged at full rates. Capital gains in respect of other assets are charged at 25 per cent.\textsuperscript{284} Capital gains are not charged in respect of agricultural lands outside urban areas.\textsuperscript{285}

\textbf{Tax Incentives}: The following are some of the more important tax incentives:

1. Depreciation

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\textsuperscript{283} See. 10 (4) ibid.

\textsuperscript{284} See. 17 (5) ibid.

\textsuperscript{285} See. 2 (4A) ibid.
In addition to normal depreciation, initial depreciation is given in the year of installation or erection at 10 per cent of the actual cost in respect of buildings, 25 per cent in respect of machinery and plant and 30 per cent in respect of ships registered in Bangladesh. In the case of new industrial undertakings set up by Bangladesh companies after July 1977 in specified classes of industries, accelerated depreciation is allowed in respect of plant and machinery at 30 per cent of the actual cost in the first year and 20 per cent in the second year in lieu of normal and initial depreciation. Where such new industries are set up in specified areas of the country, accelerated depreciation at 100 per cent of the actual cost is allowed in the first year itself. The unabsorbed depreciation can be carried forward for set off against the profits of future years.\textsuperscript{286}

2. Investment Allowance

Industrial undertakings of the type eligible for accelerated depreciation are also given investment

\textsuperscript{286}Sec. 10 (2) (via) and (vi b) ibid.
allowance in the year of commencement of commercial production at the rate of 20 per cent of the actual cost of plant and machinery. The rate is enhanced to 25 per cent in the case of industrial undertakings set up in specified areas.\footnote{Sec. 10 (2) (vii a) ibid.}

3. Scientific Research

Revenue as well as capital expenditure on scientific research related to the business of the taxpayer as well as all contributions for scientific research or technical training related to the business are allowed to be deducted in full in the computation of business income.\footnote{Sec. 10 (2) (xii), (xiii) and (xiv) ibid.}

4. Health, Education and Training

Revenue as well as capital expenditure on educational institutions or hospitals meant for the benefit of employees or their families or dependents or for training of industrial workers or for the training of Bangladesh citizens in connection with approved schemes are allowed to be deducted in full.\footnote{Sec. 10 (2) (xiv a), (xiv b) and (xv) ibid.}
5. **Tax Holiday**

Approved industrial undertakings and tourist industries set up by Bangladesh companies whose subscribed and paid-up capital is not less than one hundred thousand takas and not more than hundred million takas are entitled to a tax holiday for five years. They are, however, required to re-invest not less than 60 per cent of the tax free profits in the industrial undertakings concerned or in government bonds. In the case of similar industries set up in specified areas the tax holiday is for nine years in respect of industrial undertakings and seven years in respect of tourist industries. The limit for reinvestment in their case is 30 per cent.²⁹⁰

6. **Export profits**

Domestic companies are allowed rebates of tax in respect of export profits resulting from non-traditional exports according to the provisions of the Annual Finance Act.

7. **Export Processing Zones**

Industrial units set up in export processing

²⁹⁰Sec. 14A (2A, 2B & 2C) ibid.
zones established under the Export Processing Zone established Authority Act, 1980, are eligible for a tax holiday for five years; after that period they are allowed 50 per cent rebate of income tax on their export sales.

8. Carry Forward of Losses

Business losses, agricultural losses and capital losses can be carried forward for six years for set off against future profits.291

G- International Aspects: In the case of a non-resident any income arising from a business connection or property or asset or source of income in Bangladesh is deemed to accrue or arise in Bangladesh. So also any income from money lent at interest and brought into Bangladesh and from transfer of capital assets situated in Bangladesh.292 The provisions relating to assessment on a statutory agent, diversion of income to a non-resident and double taxation relief are similar to those under the Indian and Pakistani Laws.293

291 Sec. 24 ibid.
292 Sec. 42 ibid.
293 Sec. 43, 42 (2), 44D, 49AA ibid.
In the case of foreign technicians employed on approved contracts of service there is full tax exemption for three years. For the next five years there is tax exemption in respect of the tax paid by the employer. The value of perquisites allowed to foreign technicians during this eight-year period is also allowed to be deducted in full.

### Duties of Customs

Duties of Customs are levied under the Customs Act, 1969, which has already been mentioned under Pakistan. The import and export tariffs have been integrated with this Act. The duties are mostly ad valorem. In addition to the normal customs duties an additional customs duty is levied at 2 per cent.

Machinery, components and spare-parts imported for initial installation or for balancing, modernisation, replacement or expansion are entitled to concessional rates of duty.

Under the new industrial policy of 1982 the country is divided into developed and less-developed

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294 Sec. 4 (3) (xiii and xiii (a))

areas. In the developed areas the concessional rate of duty is 15 per cent with total exemption in respect of sales tax. In less-developed areas the concessional rate of duty is 2 1/2 per cent with full exemption of sales tax. The concessional rates admissible in less developed areas are also applicable to export-oriented (with export commitment of 80 per cent of production) and priority industries (using 70 per cent or more indigenous raw-materials) units set up elsewhere.296

Capital machinery, spares, instruments, apparatus and appliances imported for installation in an export processing zone are entitled to full exemption of customs duty as well as sales tax.297

Under a new procedure introduced298 in 1982 duty free (customs duty, additional customs duty and sales tax) import of goods is allowed


for use in the manufacture or production of export products.

Duties of Excise

Duties of excise are levied under the Central Excise and Salt Act, 1944, which has already been mentioned both under India and Pakistan. As in Pakistan, the excise duty is both on goods as well as services. Under the rationalised (1982) excise Tariff the number of items of goods and services subject to excise duty comes to 144.

Sales Tax

Sales tax is levied under the Sales Tax Ordinance, 1982, which superseded the Sales Tax Act, 1951. The tax is charged only in respect of imports into Bangladesh and in respect of a few specified exports. The general rate of tax is 20 per cent and the amount is collected along with customs duty.