THE DEVELOPMENT OF THE INCOME TAX CONSTRUCTION

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Summary

Public tribute is one of the elements of a wider category of public burden imposed by the public law norms. The elements of the sovereign imposition of the monetary obligation by the public and legal community exclude the possibility of using the term 'public tribute' to non-monetary or voluntary performance. Also, the performances resulting from all private and legal claims of the state are not regulated by the tribute law. Historically, public tributes have evolved in different economic, legal and social conditions. This explains why they do not now constitute a coherent catalogue of financial instruments which could be described with some defined, homogeneous constitutive features. The system of public tributes has evolved for the past centuries from a simple division of tributes into taxes, fees and contributions towards more complex divisions, with two clear main currents of common and specific burdens. Both common and specific burdens are currently collected in monetary form, personal servitude or tribute in kind are excluded from it. The category of common burdens covers only taxes, that is the tribute which finances state's general tasks, not based on the principle of equivalency. Specific tribute does not serve the purpose of financing the state and does not burden all the people capable of paying this performance[3].

Keywords: public tribute, income tax, theory of sources, unified income tax, unlimited and limited tax obligation

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Development of income tax public tribute

The breakthrough moment in the history of public tribute was the introduction of income tax in England. As we can see, income tax is quite a new invention. General taxes were of property type, consisting in taxing the whole property possessed by someone or its elements. Because such taxes are simple and easy to use and because taxpayers find it more difficult to hide their real estate than other taxable objects, such taxes did not require any complex tax machinery or extensive knowledge of tax collectors (officials). The forerunner of contemporary income tax was the tax imposed in England (except for Ireland) to finance the war with Napoleon, in 1799 by prime minister William Pitt (younger).

When introducing this form of taxation, the argument went that it was only temporary and it would be repealed once the war was over. The state actually resigned from collecting this tax voluntarily only once – in 1802, after finishing the war with Napoleon, Great Britain abolished this tax, after signing the peace treaty in Amiens, but for a very short period of time, as in 1803 the tax appeared again in the public tribute system at the level of 5% (the income obtained from this tax was at the same level as when the rate was 10%, this was possible by lowering the lower limit from 60 to 50 pounds which doubled the number of taxpayers). In 1806 the 10% rate was reintroduced and it was kept until 1816, when the tax was repealed again by the Parliament, a year after the battle of Waterloo, with 231 votes for and 201 against. After abolishing the tax all the data concerning taxpayers was burned (as it turned out later, copies were stored at the archives - *King's Remembrancer*). For the next 26 years the English system of public tribute did not comprise personal income tax.

The income tax introduced then had been reformed, compared to the 1799 construction, and evolved into historically the first type of income tax, the so-called scheduler tax (analytical). The construction of this tax divided all incomes into 6 schedules – groups (using property, capital, free economic activity, other capital incomes, salaries, wages), divided into 16 categories and assessed in different techniques, which all made up a single income tax, supplemented by the progressive surtax on part of the income which exceeded the statutory minimum level. As a result of these reforms and changes, income tax has been – since 1842 – fiscally the most efficient source of budget income and the most important tax in the English tax system.

The first attempts at introducing this tax in the USA were made in 1812. The British Act from 1798 was followed. Tax rates of 8% and 10% were determined (respectively for incomes exceeding 60 pounds and exceeding

200 pounds). The legislative work had nearly been completed when in 1815 the peace treaty in Ghent was signed and there was no need to introduce this tax any longer.

Just as in case of Great Britain, income tax was introduced in 1961 to finance the war operations (Civil War in the United States). Enormous time pressure to find additional sources of budget income did not allow further discussion on the sense of introducing this tax. The tax Law was signed by President Lincoln on 1st July 1982. It imposed a 3% tax on incomes above 600 dollars and 5% on incomes above 10 000 dollars. In 1864 tax rates were increased and the Americans had to pay a 5% tax on incomes above 600 dollars, 7.5% on incomes above 5000 dollars and 10% - above 10 000 dollars. The original construction of the American income tax had low tax rates, simple structure and a large amount of non-taxable income.

Italy introduced income tax in 1864, Germany in 1891, but the German construction of income tax was different from the concept of English scheduler (analytical) tax. Scheduler tax is a type of taxation consisting in separate taxation of each type of taxpayers' incomes. It allows to prefer some while discriminating other types of income by establishing differentiated scales of taxation and rates. However, it makes it difficult to use the progression with reference to taxpayers who obtain their income from a few sources. In 1891 the so-called global income tax was introduced in East Prussia. It covered the whole income of an individual, regardless of its origin. In the global tax there is no division of the tax base into incomes from particular sources, the base is just the sum of all incomes. The tax base in this system was the so-called net income, though in some cases (for example in case of taxing labor and running own economic activity) the way of establishing income from particular sources of revenue could differ. Austria introduced global income tax in its lands in 1896-1898. The Polish state income tax before the 2nd world war as well as the present personal income tax are also global in nature. Other European countries also started to introduce income taxes into their tax systems trying to obtain additional income to finance expenditure during the 1st world war.

In France and the Netherlands the income tax was introduced in 1914, in Belgium – in 1919. In France several sources of revenue were differentiated. They taxed revenues from labor and remunerations and social benefits, industrial and commercial incomes, incomes from farming, revenues from movable capital and revenues from real estate. Each of these categories was taxed separately and proportionally. The universal income tax was introduced in 1917 and was a progressive tax. In 1948 personal income tax was divided into two parts, combining two tax solutions from 1914 and 1917. The proportional rate was applied to particular categories

of incomes and revenues, in line with the 1914 solutions (global income tax) and an additional progressive rate was introduced, as in 1917 (scheduler taxes). After the reform of the tax system carried out in 1914-1917, the non-fiscal function of the income tax increased due to the introduction of various solutions taking into account the family and personal situation of a taxpayer. It was not until 1970 that the taxation of particular revenues was unified, integrating legal solutions into general personal income tax[4].

The concept of income was of vital importance in the development of income tax. We can differentiate two basic concepts of income. The first one is the concept of the theory of revenue sources focused on regular inflow of economic value from particular sources, historically linked to the English income tax. According to this theory, taxable income is a regular surplus coming from regular sources. A much broader concept of income is offered by the theory of net asset growth which combines taxable income with the growth of economic ability to spend the income, whether it is regular or one-off. The essence of this theory is the economic ability of a given individual obtained in a specified period of time and calculated by summing all net revenues (incomes) and benefits, even one-off ones (such as donations, lottery wins, etc.), obtained in one tax year. The presented theories significantly influenced the development of particular types of income tax[5].

Summing up our presentation of historical evolution of income taxes in the system of public tributes, we can differentiate three basic types of tax: Roman (mixed), German (global) and British (scheduler). The Roman type was a historical transition from revenue tax to income tax. Its specific feature lies in the fact that particular parts of income are first placed in tax schedules and are taxable according to the progressive or proportional rate, and then the general income is established and taxed according to the progressive rate. This type of income tax can be found mostly in tax systems of France, Italy, Belgium or Portugal.

Also the Polish income tax paid in 1950-1971 by individuals and legal entities which were not units of social economy was of this nature. After tax reforms in 1962, 1963 and 1974 this taxation evolved into the German type of income tax. The German type of income tax originated in East Prussia and then spread into the Netherlands, Switzerland, Austria and Scandinavian countries. In this system the tax is collected from global (general) income,

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[4] WOŁOWIEC T.: *Koncepcje pojęcia dochodu i ich wpływ na cechy podatku dochodowego od osób fizycznych w krajach strefy euro.* /in/ *Polska w strefie euro – szanse i zagrożenia*. (ed.) by J. Ostaszewski, SGH, Warszawa 2008, p. 188.

[5] MASTALSKI R.: *Prawo podatkowe II. Część szczegółowa*. ChBeck, Warszawa 1996, p.36.

regardless of the source of obtained revenues, using the progressive tax rate. In the British (scheduler) type of income tax, income is not determined globally, but partial incomes are summed, specifically defined in the so- -called schedules. The sum of partial incomes gives the total (consolidated) income. Partial incomes are taxed according to proportional or progressive rates. The tax collected from scheduler incomes is treated as an ordinary tax, contrary to the tax collected from general income using the progressive rate, which is then treated as an additional tax. Schedules determine particular incomes very casuistically, and then, within them further (detailed) division of incomes into particular groups takes place.

The evolutionary development of income tax has led to the development of several specific features dominating contemporary tax systems. The first one consists in basing the income tax construction on the theory of net asset growth, which offers its broad understanding, and, which is connected, adapting global income as the basis for taxation (freeing taxation from sources of obtaining revenue). A contemporary version of the theory of net asset growth is the theory of market income (originating in the German tax doctrine), according to which the income of a particular entity is the asset growth generated and performed by this entity. This means that income is generated only in the economic turnover, as an effect of human work, investment of capital, thus excluding inheritance, donations and other extraordinary incomes. In taxation practice, some elements of the theory of sources are also used, by excluding incomes obtained from determined sources from general income and taxing them according to a separate tax rate (usually the proportional one).

Theory of sources

Income tax based on the theory of sources (scheduler) offers far-reaching possibilities of individualizing (personalizing) taxation by determining its size to not only the size of incomes but also to their sources. This is especially visible in the British income tax. The concept of this tax is closer to the essence of income tax than the concept of tax based on the theory of net asset growth, which offers possibilities of implementing the principles of equality and tax justice. In the 20th century, in an attempt to implement these principles, revenue taxes were being replaced with income taxes. The advantage of scheduler income taxes is that they allow to adjust the taxation method and tax rates to the nature of particular income groups. This construction provides generally milder taxation of incomes obtained from work (not funded incomes) than incomes on capital (funded incomes). Using the

scheduler taxation we can achieve graduation of tax burden with reference to incomes coming from various sources and to implement the policy of the so-called just taxation.

A drawback of scheduler systems is that they do not take into account the whole financial situation of a taxpayer, that is his ability to carry the tax burden imposed on them. It is not possible to rationally personalize scheduler taxes by applying various reliefs related to particular family burdens of a taxpayer. That is why we can now witness a diversion from constructions based on a classic scheduler tax and movement towards mixed tax, in which proportional scheduler tax on particular categories of income is supplemented with global (unified) tax which progressively burdens the sum of taxpayer's incomes[6]. Moreover, scheduler tax is extremely complicated, which contradicts the requests for transparency and clarity of taxation and, due its specific structure, brings significant costs of imposing and collecting tax. From this perspective, a more appropriate construction is that of income tax based on the theory of net assets growth (global – unified – income tax). Historically this tax covered generally the whole income of an individual, regardless of the type and source of obtaining income (characteristics of particular income groups).In the construction of global (unified) tax there is no preliminary taxation of incomes from various sources, and the tax basis is a sum of incomes, however this can be calculated in different ways. Although the taxation basis was the so-called net income, in some cases (for example taxation of labor and economic activities conducted on one's own), the method of determining incomes from various sources can be differentiated.

Global, unified income tax

Global, unified income tax is a construction that is widely used in OECD countries. In the European Union, the last countries which adopted the system of global tax in 1973 were Great Britain and Italy. The construction of the global (unified) tax is more universal, as its basic elements can be applied to taxation of individuals' incomes and to legal entities incomes. Obviously, adoption of the concept of net asset growth (global income) as a prevailing concept is not tantamount to the elimination of the principle of personalizing taxation. The concept of taxing global income best implements the principle of taxing a taxpayer according to their income potential, accumulating all

[6] See more in: KALINOWSKI M.: *Współczesne systemy podatkowe.* Dom Organizatora TNOiK, Toruń 1996, p. 46 and next.

revenues of a taxpayer from all possible sources, providing a full picture the taxpayer's material situation[7]. Personal features of income tax are exposed, using the construction of the so-called existence minimum, using social and extraordinary reliefs, differentiating tax burden with the progressive scale, depending on the size of the obtained income. Personal features of global tax are also implemented by using certain elements of the theory of sources of taxation, in form of a separate taxation for incomes from some sources of revenue[8]. Taxation can be applied only to such incomes which come from regular, permanent sources, which allows to separate non-funded income (from work) from funded income (from capital, assets). For example the tax on income in form of interest on bank deposits is calculated, collected and paid out by banks themselves, thus there is no collection of advance payments and its accumulation with incomes from other sources. We should remember that the current construction of the income tax based on global understanding of income tax introduces several constraints concerning the possibility of covering losses incurred in one source of income (for example: capital investment) with income obtained from other sources (for example from remuneration), therefore it is necessary to break down the total income into its specific sources. For example, many countries do not allow to join losses incurred in high-risk investment with income from other sources. Incomes and losses from this source of revenue are accumulated as a whole and, if there is surplus in form of income – it is then added to incomes from other sources of revenue.

Personal income tax versus corporate income tax

Income tax is a prototype of personal tax – the tax which reflects the personal ability of the subjects on which it is imposed to pay it. For some

[7] See the following studies: O'DONOGHUE C. SUTHERLAND H.: *Accounting for the Family: The treatment and children in European Income Tax Systems*. „Economic and Social Policy Series", No 64 / 1998, JOUMARD I.: *Tax systems in European Union Countries*. OECD Economic Studies, No 34 / 2002, KESTI J.: *European Tax Handbook 2009-2012.* IBFD, Amsterdam 2010, 2011, 2012 i 2013; KULICKI J.*: Polityka fiskalna w Polsce w latach 1920 – 2005 w zakresie opodatkowania dochodów rodziny*. Kancelaria Sejmu, Biuro Studiów i Ekspertyz, Raport Nr 238/ 2008; KULICKI J.: *Opodatkowanie osób fizycznych. Podatek dochodowy państwach UE. Analiza porównawcza z symulacją obciążeń fiskalnych w Polsce.* Biuro Studiów i Ekspertyz Kancelarii Sejmu, Warszawa 2005.

[8] See for example MESSERE K.C.: *Tax Policy in OECD countries. Choices and Conflicts*. IBFD Publications BV, Amsterdam 1998. pp. 223 and next, MESSERE K.C.: *Tax Policy in Europe. A Comparative Survey.* "European Taxation", No 12/2000.

time income tax was only paid by individuals, as taxation of individual and legal persons was based on the same principles. For example, the companies' profits were in France (until 1948 - *impot sur les societes*) and in Great Britain (until 1965 – *corporation tax*) taxed with the tax on industrial and trade profits on the same principles as individuals. What only mattered was the fact that the enterprise existed, its legal, collective or individual nature were not taken into account. The forerunner of corporate income tax (from companies) was the construction introduced into the American tax system in 1909. It was only in 1920 that the tax systems in Germany and the United States incorporated the modern construction of corporate income tax (from companies) as a separate form of direct taxation. The introduced taxation form was a classic system of taxing company profits regardless of its destination, with additional taxation of incomes in form of dividend on the shareholder's level. The same income then is double-taxed, firstly as company profit and secondly as the income of an individual[9]. In other European countries this form of taxation developed after the World War Two. The European leader in separate taxation of individuals and companies was France, which introduced a special tax on company profits in 1948. Then the tax was introduced in Great Britain in 1965 and in Italy in 1974. Other European countries began introducing corporate income tax into their tax systems in the 1960s.[10] The following arguments supported the introduction of separate corporate income tax:[11]

1) it reduces disruptions concerning the choice of legal form of conducting business activity (companies versus individuals);
2) with reference to companies, it is impossible to use the elements of personalization, that is adjusting its construction to the individual features of a taxpayer;
3) legal persons have better paying capacity, as concentration of capital allows them to extend the size of a venture, to achieve economies of scale and to improve competitive position compared with other business entities run by individuals;
4) legal persons (companies) are not burdened with handing over property

[9] See more in OECD, *Tax and Economy a Comparative Assessment of OECD Countries*, „Tax Policy Studies", no 6/2001.

[10] See more in: GAUDAMET P.M. J. MOLINIER J.: *Finanse publiczne.* Warszawa: PWE. 2000 and next editions, pp. 472, 506 – 507.

[11] Compare, for example with: KRAJEWSKA A.: *Podatki, Unia Europejska, Polska, Kraje nadbałtyckie*. Warszawa: PWE. 2004, pp. 88 – 89. Arguments on the difficulty of integrating personal and corporate income tax: MESSERE K.C.: *Tax Policy in OECD Countries. Choices and Conflicts. Amsterdam:* International Bureau of Fiscal Documentation. 1993, pp. 325 – 326.

when the owner dies, which increases their income (tax) capacity.

It should be remembered that the most significant features of income tax are revealed in taxation of individuals. It is a tax which best implements the principle of taxation equity, through the idea of taxation equality and universality, both in the subject and in the object aspect (tax ability to pay).

The taxation of companies with income tax is a controversial issue. In case of legal persons we cannot talk of "personal paying capacity", they do not have personal needs, they do not have income "for themselves", they are only representatives of individuals. Even in conditions of tax progression there is no possibility of justifying it in the context of the theory of equal sacrifice and softening the effects of indirect tax regression.

The capacity to pay tax in case of legal persons boils down to the economic capacity, assuming that taxation cannot lead to limiting the productivity of tax sources – in the short term it should not limit economic development, in the long term – it should be conducive to this development. Therefore the measure of tax capacity of a legal person is not the income that an individual is left with to satisfy their needs, but the profitability understood as a relation of profit to own capital. Understood in this way capacity of a legal person to pay tax is firstly related to the variety of legal and organizational forms of conducting economic activity (for example taxation of single enterprises, concerns or holdings) and the purposes of their activity. As J.M. Buchanan writes: *„The differentiating feature of all systems of direct taxation can be illustrated with an elementary comparison between taxation of company income and taxation of an individual's income. In the latter, an individual changes their own tax obligation, in categories of tax burden by changes to the amount of obtained taxable income. Their own possibilities of such activity mean that their tax burden indirectly depends on the behavior of other taxpayers, who can act analogically. (...) individuals may, to some extent, lower tax burden per unit of public wealth by deciding to withdraw from investment in an enterprise. The final burden of an individual becomes inter-dependent of the activities of other people making such "investment re-allocations"*[12]. Analyzing the essence of taxation of legal persons we can notice that tax burden depends on gathering (accumulating) taxable income by a legal person, not by an individual. In order to directly reduce tax burden, such legal person would have to lower its tax base. Therefore, in order to assess its own share, even regardless of its influence on aggregated investments in the legal person sector, an individual must predict how a legal person (as a company) will

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[12] Compare: BUCHANAN J.N.: *Finanse publiczne w warunkach demokracji.* Warszawa: PWN. 1997, pp. 71 -72.

react to the height of tax burden. So we can state that there is an additional entity between the tax organ and an individual, an entity that makes decisions. We are then faced with the necessity to make new predictions, reflecting the processes of making decisions by companies (legal persons – “intermediary” entities), which are connected with most problems of group decision-making, as opposed to individual decision-making[13].

The differences between taxation of individuals and corporations do not exclude certain common elements, resulting from the fact that we tax revenues obtained by particular entities in a specific time. Particularly we can notice then analyzing material and legal construction of income tax, as well as its size and collection. The common features of income tax mostly stem from the object elements of its construction. This is mostly an indirect tax, generally related to liquid income, generated in a particular period of time, not expended income. The use of this tax (often excessive) in contemporary tax systems as one of the instruments of state interventionism accounts for the fact that income expenditure is becoming to play an important role in its construction (for example by deducting from tax base investment expenditures). We can assume that income tax covers particular inflows obtained by a given entity, minus costs of obtaining them. The notion of taxable income is very complicated itself.

For the tax definition of income it is important whether its notion should be external in relation to tax law or whether it should be an internal notion of the above-mentioned law. It is important to what extent tax income should reflect its notion in other branches of law (for example civil law), and especially its economic notion. Currently it is widely accepted that tax law is autonomous to other branches of law, as this is the requirement for achieving the goals imposed on it by the lawmakers. Therefore the notion of tax income should be as adopted by the lawmaker, therefore it cannot be an external notion in relation to tax law. It is essential for the lawmakers to base their construction on the economic category of income, which obviously does not exclude its major or minor modification resulting from the assumed goals of taxation[14].

Tax income, as ‘measure’ tax adjusted to the economic and social situation of a taxpayer, is a complex legal structure in its nature, as far as mate-

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[13] Compare: DOMAR E. MUSGRAVE R.A.: *Proportional Income Taxation and Risk – Taking.* „Quarterly Journal of Economics”, LVIII, May 1944. Reprinted /in/ *Readings in the Economics of Taxation*, (ed.) by R.A. Musgrave, C. Shoupa, R.D., Yrwing, Homewood 1959, pp. 493 – 524.

[14] See more in: MASTALSKI R.: *Prawo podatkowe II, część szczegółowa*. Warszawa: Ch. Beck. 1996, pp. 45 – 46; compare: WOŁOWIEC T.: *Koncepcje pojęcia dochodu…* op.cit., pp. 194-195.

rial law, its size and collection are concerned. It is a 'real' tax, depending on results of economic activity of a taxpayer – the course of his/her future economic activities. For implementing the goals imposed by the lawmaker on income tax it is vital to establish, through tax proceedings, the actual course of events and economic activities shaping the taxable incomes, especially determining 'the real income' and 'the real cost'.

Imposing income taxes – unlimited and limited tax obligation

Since global (unitary) income tax is a structure commonly used in contemporary tax systems, taxation of a taxpayer's income is based on the principle of tax assessment and self-calculation of tax or calculation conducted by the payer. Some factors affecting the taxation method have been selected and introduced into tax systems because of the tax purpose, depending whether fiscal burden rests on the taxpayer alone and depending on costs of administering (managing) taxes. The collection of tax from a taxpayer following the principle of tax assessment takes place after obtaining necessary information by a tax organ. If the tax is collected at source, then the entity making the payment (the payer) deducts the amount of tax and pays it into the bank account of the tax organs. This means that the taxpayer does not obtain in fact this part of income, losing the possibility of postponing the tax payment date. The payment is made 'in advance', so taking into account the changing value of money, the taxpayer loses some value of capital due to the lack of possibility of postponing the payment of income tax from the earlier to the later periods (after assessment). Therefore the taxpayer cannot – as a result of payment collection – have at their disposal the amount of tax, while the difference resulting from it – in case of some alternative investment – would allow them to obtain some additional profit (benefits), calculated at the current value of money. In the second case, when the tax is collected using the above method, it is called tax at source. Even though the tax is paid by the payer for tax organs, the recipient of this income in this case is the taxpayer.

In order to make an assessment of tax, tax organs must have reliable data (information), which is necessary when determining the amount of tax. The nature of tax assessment by tax organs imposes on the taxpayer a duty of submitting (communicating) relevant information in their tax return (declaration). If the taxpayer, despite this obligation, does not meet it, in this case tax organs are entitled to assess tax by assessing the taxpayer's income. Many tax systems resigned from the assessment method in favor of self-calculation of tax by the taxpayer. This concerns mostly corporate

income taxation, which is a situation in which tax obligation is created by law. Despite the self-calculation technique, no tax system has resigned from the obligation to submit a declaration in order to make it easier for tax organs to control the correctness of self-calculation performed by the taxpayer. This method of tax assessment is used only with reference to taxes constituting burden on the taxpayer's global income.

Since the calculation of the amount of due tax for a given tax year cannot be made before the end of the year, this means that the amount of due tax cannot be determined until the income is obtained (received or retained at the taxpayer's disposal), many countries have introduced the instrument of down-payments towards income tax, payable during the tax year, their size being determined on the basis of, for example, the amount of due tax in the previous tax year. The obligation to pay down-payments towards income tax does not change the general characteristics of the tax assessment system, which consists in determining the size of taxable income after it has been obtained.

Collecting tax at source has an unquestionable advantage consisting in the fact that tax payment is made soon after the income was given to the taxpayer's disposal (paid out by the payer). Tax collected at source may be treated as a specific down-payment towards income tax. In this method, the taxpayer is obliged to declare in his annual return form, the size of obtained income and is entitled to lower (reduce) the amount of due tax calculated in this tax return by the amount of tax that was collected at source. The tax collected at source is called 'tax paid at source included'. Alternatively the tax collected at source may be the final tax collected at source. In this case income recipient (taxpayer) is exempted from an obligation to submit tax declaration and from obligation concerning the amount of collected tax. Taxes collected at source usually have a fixed rate, which is applied to the revenue (not income), which means that we do not take into account any costs of obtaining revenue or personal situation of a taxpayer (income capacity). Therefore we can state that taxes collected at source are examples of scheduler taxes.

With reference to the income related to work remuneration, most countries combine both methods of collection, that is assessment and collection of tax at source, which is known as the 'pay as you earn (PAYE) system. In this system, employers (payers) are obliged to collect tax at source from remunerations of their employees. Contrary to taxes collected at source, tax collected from remuneration is not collected at a fixed rate, which is typical for the system of collecting tax at source. Generally, the amount of tax collected at source from remuneration reflects personal situation of taxpayers, and the taxpayer is obliged to inform the employer (payer) of

their personal situation if it affects the size of their tax burden, in order to allow the payer to apply appropriate system of down-payment collection. In a situation when the system of collecting tax from remuneration is used properly, taxpayers are exempted from the obligation to submit tax declarations, if they do not obtain any other income or if they obtain income from other sources of revenue which is subject to final tax collected at source. In most EU and OECD countries which use the above system of down-payment collection, we can observe a downward trend in tax inflows, which calls for activities aimed at introducing the obligation to submit tax returns by taxpayers (employees) in order to allow tax organs to control the appropriateness of due tax calculation.

Most countries tax all incomes obtained by their residents, regardless of the location of income source, thus creating a category of unlimited tax obligation. Numerous factors affecting the state's tax policy regarding its residents account for the fact that residents are subject to taxation on the basis of assessment method. For example, countries which make their tax claims against residents are often interested in implementing, to some extent, the principle of vertical equity. The state's tax policy regarding residents also contains some elements of income redistribution function. These assumptions are reflected in principles governing taxation of individuals, which means that tax burden related to individuals depends on their personal situation.

With reference to incomes from conducted economic activity, tax assessment made by tax organs is necessary due to the fact that tax is a burden on income, not revenue, therefore taxpayers who conduct economic activity are obliged to declare the size of revenue and expenditure constituting costs of obtaining revenue. In special situations the tax on economic activity may be calculated on a different than net income base, for example on gross revenue (inflows from this activity), but this type of tax also – in principle – obliges taxpayers to submit tax declarations.

Although residents are taxed on the basis of tax assessment method, countries often introduce the method of collecting tax at source in order to streamline tax collection process. In this situation, a system of down-payments towards income tax is introduced, in order to collect income tax as early as possible (for example tax on dividends paid out by a company with registered office in a given state to shareholders who are not residents of this state related to gathering means on savings accounts in a bank which is the resident of this state). Tax collected at source in form of down-payment is also imposed on this category of incomes, in which there is high risk of not declaring for taxation or in which taxpayers could avoid taxation in any other way.

Tax organs of a particular country may impose final tax at source on incomes of its residents in case when these incomes have been excluded

from tax assessment base. Such approach may lead to simplification of tax collection. The mechanism of the final tax collected at source is very simple to use, therefore the more categories of taxpayers' income that can be taxed in this way, the less time is spent on the procedure of tax assessment. Moreover, the rate of final tax collected at source may be determined on a relatively low level, which additionally encourages taxpayers to save or invest. Thus we can state that final tax collected at source burdens incomes of individuals from minor investment[15].

There are many variations of residence-based taxation, such as taxation on remittance basis which is used in some countries with common law systems. In this system incomes from overseas sources are subject to taxation insomuch as they have been transferred to the resident state of a taxpayer. This means that income from these sources is taxed at the moment of remitting or transferring it to the resident state in form of money transfer, transfer of elements of assets purchases with income obtained from foreign sources for repayment of debt in the taxpayer's resident state. This principle is used with individuals (residents) who are strongly tied with foreign countries, for example people who have just become subject to unlimited tax obligation in the resident state.

The term "taxation at source" is used – in principle – with reference to taxation of incomes obtained by non-residents of one country from sources of revenue located in this country. This type of tax obligation is known as limited tax obligation, as the scope of tax claims of a given state is limited only to incomes from sources located in this country.

Using the principle of source, the state is in a totally different situation than in case of taxing incomes on the residence basis, especially when it comes to taxation of non-residents who obtain only incomes from dividends, interests or license fees whose source is located in this country. Such income source state may have limited information on taxpayers who are not its residents, therefore it cannot demand that they fulfill their obligation of submitting tax return or that they pay tax at a later date (for example at the end of tax year), as (when enforcing its claims against non-residents) it risks

[15] See more: WOŁOWIEC T. SOBOŃ J. ROGOZIŃSKA-MITRUT: *Some issues of personal income taxation.* Winnica: INSTITUTE OF UKRAINIAN – POLISH COOPERATION 2012. ISBN 978-617-530-083-1. pp. 132.; WOŁOWIEC T. ISMAILOVA D. ROGOZIŃSKA-MITRUT J. (ed). *New trends in social policy and welfare economy.* Kiyev: INSTITUTE OF UKRAINIAN – POLISH COOPERATION 2012. ISBN 978-966-2696-15-8. pp. 422; SULŻYCKI Z. WOŁOWIEC T. ROGOZIŃSKA-MITRUT J. *Ewolucja systemu danin publicznych*. /in/ WOŁOWIEC T. (ed.) *Wybrane problemy teorii i praktyki opodatkowania*. Kiyev-Świnoujście: Cech Rzemiosł Różnych & Institute of Cooperation in Kyiev 2012, ISBN 978-83-934895-4-1. pp. 13-24.

infringing sovereignty of another country. In this situation the income source state is primarily interested in effective collection of tax, preferably before the income is transferred to non-residents abroad. The best solution seems to be offered by tax collected at source, as it can be collected even when the income source state does not know personal data of income recipient, as obligation to collect tax is placed on the payer (who pays the income), which is usually the entity that is subject to unlimited tax obligation in the country of the source of income paid abroad. The application of tax at source to dividends, interests and license fees obtained by non-residents is mostly seen in form of final tax collected at source.

The legal and tax situation of non-residents changes when they are strongly involved in the activity in the territory of the source state, as in case of activities run by foreign companies through the factory located in the source state. The degree of non-residents' involvement is then considered sufficient to tax them on the same principles as residents are taxed. The state imposing the tax may then, without any restrictions, demand that they fulfill their obligation of submitting their tax return (declaration), as non-residents have their residence addresses in the source state, are obliged to register their activities in the source state and notify tax organs of taking up activities, which is a necessary condition for conducting activities in a source state. Thus the source state may require the non-resident running their activity through a factory located here to submit a tax return (declaration), so it is possible to assess tax on net income by tax organs. In a situation when a non-resident obtains income in form of dividends, interests or license fees through the factory and when the tax at source was collected on these categories of income, incomes from these areas – generally – are joined with the factory incomes from other sources, while the already collected tax is put towards due tax on total incomes of the factory. There is no doubt that the construction of taxation at source rules in conditions of limited tax obligation is consistent with the idea of taking global tax as tax base by making taxation independent from sources of obtaining income.

Some countries impose additional tax, known as branch tax, on incomes obtained by non-residents through the factory. The purpose of this tax is to achieve a situation in which a foreign company enjoys the same legal and tax situation as in case of having an affiliated company instead of a factory in the territory of a source state. An affiliated company is subject to income tax on obtained income, while dividends it pays to its parent company are taxed at source. Tax on branch income is an equivalent of tax at source collected from dividends. Usually it covers global profits of a factory after their taxation with income tax. It should be remembered though that in practice some countries impose this tax only on factory profits that have not been

invested into factory's fixed assets. It also happens that countries use the method of taxing the part of factory profits which has been transferred to the company headquarters[16].

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[16] See more in: HAMAKERS H. HOLMES K. GŁUCHOWSKI J. KARDACH T. NYKIEL W.: *Wprowadzenie do międzynarodowego prawa podatkowego*. LexisNexis, Warszawa 2006, p. 33.

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