

DEVELOPMENT OF THE TAXATION SYSTEMS IN JAPAN AND TURKEY

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1. Introduction :

The aim of this paper is to analyze the development of the taxation systems in Japan and Turkey in general. Besides giving a general description of the development of the systems in both countries, it is also aimed to point out the apparent disparities in the developmental paths in the two countries.

The idea in analyzing the tax systems of these two countries is to make a comparison between these countries which have similarities in certain aspects. Indeed, both Japan and Turkey have been exposed to western civilization during the stage of their economic backwardness, though the time and style of exposure has been quite different. Japan had been forced by westerners, especially Americans, to open the country to western traders after almost two hundred years of seclusion. The merits and demerits of that long-lived seclusion period are beyond the scope of this paper.

Turkey, on the other side, had always been in close contact with European nations, though without benefiting from their techniques and know-how throughout the whole period till the last years of the Ottoman Empire. However, towards the end of the Empire period, some efforts had been made to adopt western techniques, but the never ending wars prevented the Ottomans to make real steps in that direction.

The establishment of the Turkish Republic enabled the political leaders to focus on the problems of westernization and industrialization. Some modernization attempts had been made, such as the changing of the mode of living, the style of customs, the changing of the Arabic letters into Latin alphabet, etc. Those reforms were imposed upon the society. However, the infrastructure of the society both in economic and social senses was lacking to a great extent. Almost three-quarters of the population was illiterate at the time. The accumulated capital consisted of a few factories inherited from the Ottoman Empire which were producing mostly for the needs of the army. As for entrepreneurs up to western standards, there were almost none. Hence Turkey tried to initiate western reforms upon that structure at the beginning of the 1920's, with due qualification for some efforts made during the Ottoman period.

The picture in the above sense is quite different in the case of Japan which followed a somewhat different developmental path in her social and economic history. At the beginning of the Meiji Era, which can be considered as the backbone of Japanese economic development efforts, the literacy rate was around 40%. In the Tokugawa Era education was given a great importance (1).

As to the Japanese economic and entrepreneurial history, the situation during the opening years of the Meiji Era was better than it was in Turkey in the 1920's. Some families had been distinguished in Japan as industrial families, generally coming from the merchant class in the Tokugawa Era. The capital accumulation was sufficient to enable the government to hand over most of the state economic enterprises to the private sector in 1882 (2). The selling of the state economic enterprises to the private sector at a price much lower than their genuine values then had some implications, but in any case this fact shows the economic power of the private sector at that time.

The Japanese Economy was also monetized to a considerable degree at the beginning of the Meiji Era. The percentage

of the agricultural product marketed and the adoption of the taxation show the degree of monetization in the economy (3).

The policies which had been followed in Japan and Turkey in different periods had, no doubt, different impacts on the development of the economies in these countries. The social factors, such as social relations, customs, religious factors, etc., had also affected the development of the countries in different ways.

The object here is not to trace all the relevant factors and their impact on the development of the countries. Instead, what is aimed in this paper is just to follow the developmental path of the taxation systems and find out certain correlation between the taxation systems and the economic structural change in both countries. Therefore, we shall not deal with the factors affecting the economic conditions, but we will only emphasize the development of the taxation systems and their relation to basic economic changes that had taken place in both countries over time.

As to the time period covered in the paper, it is difficult to take the same time segment for the two countries, because they had reached different stages of development at different time periods. It is, therefore, necessary to fix different time periods for each of the countries. For Japan the time period covers the late years of Tokugawa Period, the Meiji Period, the pre-war and post-war periods up to the 1950's. Up to the Shoup mission there had been considerable changes in the taxation systems in Japan, both in the kinds of taxes employed and in the methods of assessment. After the 1950's the system had also undergone some changes, but those recent changes do not count much in the matter.

For Turkey the case is somewhat different. In the 1920's the Ottoman Empire was demolished, and the new Turkish Republic had emerged out of ruins caused by endless social and political unrest in the decaying period of the Empire. The

leaders of modern Turkey, no doubt, tried to adopt new systems in every way, but some old systems lived for some time in the Republican time. It is, therefore, necessary to make a brief review of the Ottoman tax system. Then we can turn to the developments realized in the Republican period. Like Japan, in Turkey, also, considerable changes had taken place almost up to the 1950's. The changes since then have less significance in the matter. Accordingly, we shall emphasize the developments up to the 1950's, while giving a brief explanation for the changes made after the year 1950.

In the following sections, the development of the taxation systems in Japan and Turkey will be surveyed according to the above explanation.

2. Development of the Taxation System in Japan:

In this section the development of the taxation system in Japan will be introduced in three sections. In the first section, the taxation system of the Tokugawa period will be examined briefly. In the second section the Meiji Period taxation system, especially the land tax system, will be analyzed. Finally, in the third section, the post-Meiji period and the post-war period will be examined.

a. Tokugawa Period:

During the Tokugawa Period the economy was not exposed to market transactions to a great extent and rice was the only important means of measurement for wealth. Almost everything was expressed in terms of quantities of rice. Thus, the Tokugawa Period had been known as the age of rice economy (2). The taxes were paid in kind as well.

The society was composed of four classes, the daimyo or hans who were administrators in general, the warriors who were called Samurai, the merchants, and, finally, the farmers.

The economic wealth was believed to be produced by the agricultural sector only. Merchants had been considered as parasites on the society. Therefore, the taxes had to be levied on the agricultural sector because that sector was the only one making real production.

In the Takugawa Era mainly three types of taxes had been employed. They were denso, komononari, and kayaku (5). Denso was the most important revenue item in that period. More than half of the annual yield used to be given to the daimyo or han as tax. This was a tax on agricultural production. Two methods of assessment had been employed. In the first method a fixed assessment system was employed, whereas in the second system an annual assessment system was employed.

The second tax, komononari, was a tax on forests, waste land, rivers, etc. In this tax, also, different assessment systems had been employed.

The third tax was a kind of poll-tax. The tax-payers had to work in certain unpaid jobs as coolies. If the tax-payer refused to give his service as a coolie, then he had to pay certain amount of money in lieu of his service. Thus that was a tax paid in cash.

Besides these three main taxes some other small taxes had been used, too. The most important of that class of taxes was goyokin which was actually a tax on merchants. But, sometimes farmers also had been asked to pay goyokin.

The system described above has the characteristics of the system of an agricultural economy. The burden of the taxes was heavily on the agricultural sector. According to Honjo, the relative tax burden distribution among different classes was as follows; agricultural class 84 %, samurai class 12 %, and merchant class 4 % (6).

The relatively heavy burden on the agricultural sector and the samurai class made them react against the merchant class. The enhancement of the economical position of the merchant class aggravated the temperament of the other classes against

the merchant class. Thus, towards the end of the Tokugawa Period there had been some proposals to tax the merchant class more heavily. Some proposals even envisaged a 50 % tax on them. However, the tax proposals and the modernization proposals of the Tokugawa administration could not be implemented and at the end of the Tokugawa Period there was almost no important change in the relative tax-burdens on the different classes.

b. Meiji Period:

The period between the years 1868 and 1912 is called the Meiji Era in the Japanese history. This period has the utmost significance from the viewpoint of social and economic development.

The main tax that the Meiji Era inherited from the Tokugawa Period was the famous land tax, which had hitherto been implemented as a tax paid-in-kind. There were also some unimportant taxes yielding high revenue.

Among many other social and economic reforms that had been implemented during the Meiji Period we consider the advanced steps that had been taken in the way of improving the taxation system to suit it best to the economic needs of the time. The compelling forces for the Meiji leaders to make reforms in taxes were not only economic needs, but also the increase of the government outlays to settle the political unrest in the country. Indeed, the Meiji Restoration did not take place in a quiet atmosphere. Rather there were many political problems as well as rebels sometimes. Besides, the Meiji Administration had shouldered the samurai stipends as well as most of the debts of the Tokugawa hans. Therefore, the financial problems were, perhaps, the most outstanding issues facing the Meiji Leaders. Thus, they turned the attention to the taxation issues, especially the land tax problem.

In 1873 a bold reform was launched in the field of land taxation. That reform had three significant principles: 1) The

new tax had to be assessed on the value of land, whereas the tax-base was the harvest in the Tokugawa period; 2) The rate was fixed at 3 % in the beginning and later reduced to 2,5 %; 3) The tax was to be collected in cash, whereas it was collected in kind in the Tokugawa Era (7). The initial difficulty was the assessment of land values. According to the first version of the law, the «legal value» of the land had to be determined by the average yield of each piece of land during five years at the average price of rice. Then, that sum had to be capitalized to reach the legal value of the land. And the reassessments had to be made at every six years. But the plan was not put in effect (8). Instead of this rather complicated plan, a simple one was adopted. According to that plan the assessment of a land value should be made by multiplying the crop yield in money terms by 8,5 (9). The fixing to the tax-base as described above and the tax rate at 2,5 % yielded a stable revenue to the government, though only in monetary terms. The increase in the price of rice had a two-sided effect both on public revenue and after-tax income of tax-payers. As the price increases affected the purchasing power of money, the public revenue became progressively smaller in real terms. On the other hand, the same mechanism enabled the land owners to pile large economic surpluses.

The government did not stay silent in the face of increasing prices, but severe anti-inflationary measures were put in effect by famous Matsukata. During his term of office the volume of money was reduced and the general price level in 1884 was lowered to almost 75 % of the price level of 1881 (10).

The evaluation of the impact of the land tax reform of 1873 together with the Matsukata deflation is somewhat interesting. The first influence of the tax, which was changed into cash payment system, was the diffusion of market economy and the increase of the degree of monetization of the economy (11). The second interesting influence of the new form of tax was the concentration of land ownership in certain hands. The mechanism was as follows: The fact that the tax-payers were land-

owners officially forced the small farmers to borrow money from big and wealthy farmers in order to pay taxes, especially in the first years of the reform, before the deflationary policy was put into effect. As the result of such borrowing many small farmers lost their lands through foreclosure (12). To give a numerical example, the following situation can be cited. The land-tenancy increased to 40 % in 1892 from its 30 % level in 1870 (13).

Still another aspect of the policy which further decreased the real income of small farmers was the adoption of common lands as subject to private ownership. Through this policy the real estate of the Emperor and the high rank governors increased tremendously, while small farmers were prevented from benefiting from those lands in getting wood, etc any more (14).

As to the effect of land tax reform on the urban-rural distribution of the population, it is quite safe to say that the tendency had been towards urbanization. The high burden of the land tax had forced some of the agrarians to sell their lands and move to newly developing industrial centers. The indices given below show us the degree of urbanization and changes in the agricultural labor force (15).

Table — 1
Indices of Urbanization and Agricultural
Labour Force

Years	Urbanization	Agricultural Labour Force
1887	100.0	100.0
1891	111.3	99.2
1895	122.1	98.4
1899	152.7	97.5
1903	142.8	96.8
1907	152.8	96.1
1911	162.6	95.4
1915	171.9	94.7

Before going on with other taxes employed in the Meiji Era, the following table will help us to evaluate the relative importance of the land tax in the general revenue system in that period (16).

Table — 2
The Share of the Land Tax
in Total Revenue

Years	Share
1870	39.2 %
1871	51.1 %
1872	39.6 %
1873	70.8 %
1874	80.9 %
1877	82.5 %
1897	42.4 %

Undoubtedly, the land tax was not the sole source of revenue of the Meiji Era. Other than the land tax, there were the income tax, enacted in 1887, a general tax on business turnover and capital, enacted in 1896, and a modest inheritance tax which was enacted in 1905. Leaving the other two taxes aside, we will now focus on the income taxation problem, because as the economy grows and proceeds in industrial and commercial branches, income taxation gains importance. Therefore, the role of the land taxation, which was also a type of income tax, shifts gradually to income taxation in the modern sense. This fact can also be observed in Table-2 in the decreasing percentage of the land tax, implying the increasing importance of other taxes, mainly the income tax. Therefore, from now on we shall concentrate on the development of income taxation in Japan.

The first income tax law enacted in Japan in March, 1887. Up to that time Japan had employed her traditional taxes, namely the tax on land and the tax on liquer, etc. Similar to almost all other taxes, the income tax had been the consequence of pressing ever-increasing government expenditures, mainly

war-related expenditures, such as the expenditures needed for the expansion of naval forces (17).

The first income tax was a modern version of taxation for that time with some interesting articles, such as the averaging of income for three years, which was a somewhat complicated method compared with bookkeeping methods and capacities of tax authorities of the time. However, in 1926 the calculation of income was changed into the actual income of the preceding year.

After the 1894-95 Sino-Japanese war the government tried to revise the prevailing taxes, income tax as well, in order to increase the revenue to cover the war-related expenditures. The first step that the government tried to take was to split the corporate incomes, mainly dividends, from the earnings of corporations and reach two of them separately by two different taxes. Hitherto, the corporate incomes were taxed, but dividends were exempted from the income tax. In order to achieve that goal a drastic change in the income taxation system was necessary: a corporation income tax should have been introduced along with the income tax. However, facing rather strong opposition from different circles, mainly from business and industrial centers, the government was not able to proceed so boldly. There was also a fear of hampering capital accumulation on the side of government officials. For this reason, the 1899 tax reform came out without fully realizing the initial aims of the government. In that law the incomes were classified under three sections. In the first section corporate incomes were covered. In the second section interest on bonds and debentures were covered. Finally, in the third section other miscellaneous incomes were covered (18). Thus, dividend incomes remained untaxed.

In the very first year of the twentieth century, the Boxer Rebellion and after four years, in 1904-1905 the Russo-Japanese war compelled the government to expand her outlays so extensively as to establish an extraordinary military special account

to cover those outlays (19). Thus, in 1903 came the emergency special tax increases. In the reform movement, corporations were split into two main classes according to their type of partnership and size and the tax rates were made progressive. However, individual incomes gained from bonds and debentures, class II income, were kept untouched. It was a rather wise policy to lighten the tax-burden on public debts during a period in which government was greatly in need of money and could resort to bond financing any time. In February, 1905 all interests earned on government bonds were exempted from taxation (20).

c. Post-Meiji Developments:

The First World War was the first important event in the post-Meiji Era. The war affected the governmental fiscal policy as the other wars had before. As a result, in 1913 and 1918, two main revisions took place mainly in the field of income taxation. Income brackets were readjusted, tax rates were somewhat increased, extra brackets for individuals and corporations were assumed. The 1913 and 1918 revisions were not only in the way of increasing tax rates, but also there were some efforts to modify the tax burden in the face of growing inflation on especially low-income groups by assuming higher exemption limits.

Income tax had been subject to various changes between 1920 and 1940, sometimes to the changing economic conditions and sometimes to finance the expanding government outlays. For instance, an extra-ordinary profit tax was passed in 1935. This tax was imposed on incomes exceeding the average income of business units.

While coming to the major tax reform of 1940, we consider several attempts to raise the tax revenue. Among them are the Temporary Tax Increment Law and some other tax increases to cover the Special Account for Expenses. However, none of those attempts could succeed in providing the government with a reliable source of revenue. Thus, in 1940, a broader-viewed reform was set off. The aims of that reform were the following:

1) Achieving an equitable distribution of the tax burden; 2) Adjustment of the tax system according to economic ends; 3) An elastic and a high yielding tax system; 4) A simple tax system (21). The heavy relative share of the indirect taxes (about 60 %) in the 1940's compelled the authorities to give a more emphasis to direct taxes. Thus, a revolutionary revision in the field of income taxation took place in Japan in 1940.

First of all, individual and corporate income taxes were separated from each other, whereas corporate income had been treated within a single income tax law till then. According to the 1940 reform, the individuals would be subjected to the individual income tax law, while the corporations would be the tax-payers of the corporate income tax law. The individual income tax was a double-form tax, in the first stage individual incomes were taxed separately at flat rates, though the rates were different for various classes of income. Income was classified as follows: real estate income, dividends and interest income, income from enterprises, labor income, income from forestry enterprises, and retirement allowance income (22). The proportional rates changed between 5 % and 40 %. On this schedular basis there was a global income tax which was applied progressively, the rates changing from 10 % to 65 % on individuals who had a total income of 5,000 or more.

Necessary allowances in the taxation system gave a somewhat disguised progressivity to the schedular income tax law, too.

The adoption of the global income tax on the schedular income tax prevented the local authorities from levying a local surtax on the national income tax which they were experiencing till then. This had been considered as a step towards fiscal centralization. The changing of the land tax, the house tax, and the business tax into national taxes had the same effect, too (23).

The corporation income tax was a flat-rate tax, the rate being 18 %, and imposed on the earnings of corporations. The 1940 reform also altered the treatment of the corporation tax

within the cost element of the firm. Hitherto, the tax on corporate earnings had been deducted from the gross revenue of the firm. Correctly, that method of deduction was abandoned in the 1940 reform. However, the new system, undoubtedly, increased the tax burden of the tax-payers and the relative share of the direct taxes in the total tax revenue. After 1940, the relative share of direct taxes in the total revenue increased to 64.1 % from its previous share of 34.3 % (24).

Of course, certain other direct taxes, such as extraordinary profit tax and real estate tax that were initially employed in that period contributed also in the increment of the share of direct taxes.

Until 1950 some reform movements had been seen. The most important of them can be cited as follows: In 1946 a property tax, to be imposed once only, was enacted to check inflation. However, the tax did not succeed in checking inflation. In 1947 the schedular income tax was replaced by a progressive comprehensive income tax. In 1947, the current year's income was accepted as the tax base in the income tax law. Finally, in 1948 a turnover tax, imposed on every stage of transactions at the rate of 1 % was enacted. But it was abolished in 1950.

During the war period mostly indirect taxes adjusted to raise revenue to cover war related expenditures. Thus, the relative share of those taxes started to increase after a temporary low level during the 1940's. The share of indirect taxes increased to 45.9 % in 1949 from its level of 35.9 % (25).

In 1950 Japan undertook a second big reform in her taxation system according to the recommendations of the Shoup Mission. Previously, some rather administrative measures were implemented in line with the Dodge Plan. But the Shoup Mission had a more comprehensive impact on the Japanese taxation system. The general philosophy of the Shoup Mission recommendations can be summarized in the following headings: 1)

Simplification; 2) Individualism; 3' More emphasis on the local taxation system. Those characteristics were contradictory to Japanese customs which have always given much emphasis to nationalism and centralism. However, the tax authorities made enormous changes in the general tax system.

In the field of income taxation, all incomes, including capital gains, were covered at rates changing from 20 % to 55 %. Thus, the highest rate of income tax had been reduced from 85 % to 55 % to encourage business investments and to increase the labor force (26). However, the inclusion of capital gains was detrimental to the development of the securities market because of the lock-in-effect of the tax. For that reason, in 1953, the capital gains were excluded from the general income tax and a new levy for that special income item, called the securities transaction tax, was enacted. That new tax, no doubt, could have the same lock-in-effect, but, depending on the rate of the tax, that effect could be much smaller.

In addition to the income tax, a net worth tax was introduced at rates 0.5 % - 3 %.

The corporation income tax rate had been fixed at 35 % and undistributed profits were taxed at 2 %.

There had also been some changes in the indirect taxes, mostly in the direction of decreasing their numbers.

Thus, the reform of 1950 emphasised mostly direct taxes, making some small changes in indirect taxes.

To give an idea about the changes in the national tax system made after the Shoup Mission, the following table has been introduced (27).

Table — 3

National Tax Systems Before and After
the Shoup Recommendations

1948	Revenue Taxes	1951
Income Tax		Income Tax
Corporation Income Tax		Corporation Income Tax
Special Corporation Income Tax		Accession Tax
Real Estate Tax		Net Worth Tax
Capital Levy		Revaluation Levy
War Indemnity		
Circulation Taxes		
Securities Transfer Tax		Bourse Tax
Transactions Tax		Commodity Tax
Bourse Tax		Tonnage Duties
Commodity Tax		Travel Duty
Tonnage Duties		Registration Levy
Travel Duty		Stamp Levy
Horse Racing Levy		
Registration Levy		
Stamp Levy		
Consumption Taxes		
Liquor Tax		Liquor Tax
Soft Drinks Tax		Soft Drinks Tax
Monopoly Profits		Monopoly Profits
Sugar Excise		Sugar Excise
Textile Excise		Playing Sets Tax
Playing Sets Tax		Gasoline Tax
Customs Duties		Customs Duties

One important element of the 1950 reform was the introduction of the revaluation system for assets. This was very important, especially in periods of high price increases. Otherwise, the depreciation allowances would not be able to cover the total replacement costs. The revaluation was optional for business firms. It was compulsory for individuals during the transfer of assets. The surplus gained as the result of revaluation was taxed at 6 % rate (28).

The other very striking feature about the Shoup Recommendations was the adoption of a value added tax at the prefectural level, but the tax was never put in effect (29).

The effect of the Shoup Recommendations on the relative weights of the national and local taxes can be seen in the following table (30).

Table — 4

Relative Shares of National
and Local Taxes

Years	National	Local
1928	45.9 %	54.1 %
1949	45.0 %	55.0 %
1950	42.9 %	57.1 %
1951	42.0 %	57.6 %
1952	42.4 %	57.6 %

After the adoption of a new system in accordance with the Shoup Mission Recommendations, many debates took place on the national level to change the system to adapt it more to the Japanese customs. Thus, in 1953, another wave of reforms was enacted. That year the net worth tax was repealed because of its unfavourable effects on tax equity. Income tax rates were increased, the highest rate being 65 %. Capital gains were excluded from the income taxation and a special tax. Securities Transactions Tax, was enacted to cover such incomes. Inheritance tax was split into two as inheritance tax and gift tax.

Though so many changes in the tax laws were made, the main system was kept intact.

The changes made in the taxation system following the 1953 reform produced complications. To give an example it can be said that there are many income taxes today; income tax, corporation income tax, prefectural inhabitant tax, enterprise tax, and municipal inhabitant tax (31).

Before we finish the section on the development of the Japanese taxation system, we shall make a general evaluation of the functioning of the main taxes. The following tables have been introduced for that purpose (32).

Table — 5

Relative Weights of Direct and Indirect Taxes

Years	Direct Taxes	Indirect Taxes
1935	34.3 %	65.7 %
1941	64.1 %	35.9 %
1950	54.9 %	45.1 %
1955	51.4 %	48.6 %
1960	54.3 %	45.7 %
1965	59.2 %	40.8 %
1969	62.7 %	37.3 %

Table — 6

National Income Elasticities of Various Taxes

Years	Total Tax Yield	Income Tax	Corp. Inc. Tax	Indirect Taxes
1957	1.70	2.38	2.43	0.65
1960	1.70	2.22	2.35	0.97
1962	1.74	3.42	1.37	0.96
1964	1.16	2.06	0.89	0.74
1966	1.36	2.19	1.24	0.90

In Table-5 it is observed that the relative weight of direct taxes has always been over 50 %, which is a significant means of tax-equity.

As to the income elasticity of taxes, Table-6 shows that the total tax yield has always shown an elasticity coefficient greater than one. The income tax ranks in the first row in having the highest elasticity coefficient. It is natural for the income tax to have such a high elasticity coefficient because of its progressive and built-in-flexible structure. Corporation tax has also performed quite well. But, indirect taxes have a coefficient less than one.

3. Development of the Taxation System in Turkey:

Since Turkish Republic is an extension of the Ottoman Empire and some of the Ottoman tax laws had been used during the beginning years of the Turkish Republic, it is important and useful to have some idea about the general taxation system employed in the Ottoman Empire in general. The following section is, therefore, divided into two subsections. In the first part a general evaluation of the taxation system employed in the Ottoman Empire will be made. Later on we shall continue, in the second part, with the explanation of the developments in the tax system in Republican Turkey.

a. Ottoman Empire Period:

In the Ottoman Empire, the taxation system, as well as the administration system was of a religious character. In that system the citizens were divided into two broad classes according to their religious denomination; Moslems and Non-Moslems.

The second characteristic of the taxation system was that it rested mainly on the agricultural sector which then provided almost the three-quarters of the GNP.

The methods of tax assessment and collection were somewhat obsolete. Thus, they created discrimination and certain administrative problems both for the tax-payers and the tax-authorities. The state had used the tax-farming method through adjudication. Tax-farmers were generally obliged to pay a fixed amount to the state. The difference between the actual amount collected from the tax-payers and the amount agreed-upon according to the adjudication agreement between the central government and the tax-farmers was the net gain or loss to the tax-farmer. Thus, that method had always led the tax-farmers to exert pressure, even sometimes illegally, upon the tax-payers in order to collect the maximum amount possible.

The tax had to be paid in kind according to the value of the agricultural product. The tax-farmers used to levy the tax during the harvest period so that there was no way of tax evasion for the tax-payers except illegal bargaining procedures which generally ended in favour of the tax-farmers.

This system had the advantage of providing the state with a stable revenue source, though it had several disadvantages on the side of both the state and the tax-payers. However, lack of modern means of transportation and communication had obliged the state to resort to such an obsolete system.

The tax rates were different, depending upon the tax-payers' religious denomination; non-Moslems were being applied higher rates. This differential rate structure had two important political implications. The first one was the encouragement felt on the state side to implement a somewhat old-style imperialistic policy. Since the conquest of new areas which was inhabited by non-Moslems enabled the state to collect a higher tax revenue, the state did not hesitate to enlarge her frontiers whenever she felt herself militarily strong. The second political impact of the tax levied on non-Moslems was that the state tolerated the religious belief of the people in the newly conquered areas. In other words, no pressure was applied to them to become Moslems. No doubt, the sole factor of these policies was not the

differential rate structure. But the rate structure encouraged the policies then implemented.

These two political consequences had constituted the reasons, besides others as well, for the destruction of the Empire herself. The first impact made the Empire to enlarge so far as to trespass the optimal administration limits available then, while the second impact brought about a nation of somewhat heterogeneous character.

The following table summarizes the general taxation system of the Ottoman Empire in the closing years. It also provides us with the percentage distribution of various taxes that had been used then (33).

Table — 7
Ottoman Empire Receipts
Fiscal Year, 1911-12

<u>Revenues</u>	<u>Percentages</u>
Land Taxes	9.2
Military Exemption	5.8
Payments in Kind	2.0
Livestock Taxes	6.7
Tithes	25.2
All others	1.6
Stamps, fees, etc.	4.6
Indirect Taxes	17.7
Customs	14.7
Monopolies	11.8
Salt	4.2
Tobacco	3.3
Post, telegraphs, telephones	3.0
All others	1.3

(Continued on page 57)

Table — 7 (Continued)

State Enterprises	0.8
State Domains	2.6
Tribute	2.8
Repayment of Advances by the State	0.2
Reserves for Pensions	3.5
Miscellaneous	5.5
	<hr/>
	100.0

The most striking feature about the Ottoman Treasury system was its heavy dependence on tithe which was a kind of agricultural income tax levied on the crop yielded each year. The second important income tax was land tax, which was another direct tax assessed on the value of the land. Customs taxes also constituted a high percentage in the total revenue system. Tribute, which had hitherto been important, had lost its importance in revenue system as the Empire had lost most of her domains inhabited by Non-Moslems.

b. Republican Turkey Period:

The destruction of the Ottoman Empire and the emergence of modern Turkey in the 1920's compelled the new government to cope with many difficult problems, both economic and political. No doubt, the revision of the taxation system inherited from the Ottoman Empire was not the most important of all. After all, there was a taxation system which had been used up to that time and the new government was not strong enough to make radical changes in the system. Therefore, in the very first years of the Republic no major change in the taxation system had taken place. Almost all the legislative activities of that period were confined to the legalization of the old taxes in the Republican Parliament. For this purpose some tax laws had been enacted stating that the tithe, the agricultural tax, and a somewhat obsolete tax on incomes gained besides agriculture, mainly

trading incomes, were to be implemented without significant changes.

To recapitulate, we can state that mainly two kinds of income taxes were in use, one on agricultural incomes and the other mainly on trading incomes. The taxes were of religious origin. The Republican Government adhered to the Ottoman taxation system in the very first years without making any changes.

In the first years of the Republic, an extraordinary tax on windfalls was implemented. This was to channel some part of windfalls that individuals had acquired during war periods to the public sector. It was a short-lived extraordinary tax.

Another tax of the same period, which is worth mentioning in order to reflect the taxation philosophy of that period is the poll-tax that could be paid either in cash or in kind; the taxpayer had the option of either working for the state for four days a year or paying the equivalent of four workers' salaries to the government.

The first important change came in 1925. The main agricultural tax which had been implemented during the Empire period had been rebated in that year without establishing any other tax to substitute for it (34). In 1924, the last year of the implementation of the tithe, the tax revenue was about 12 million Turkish Liras, which was about the 20 % of the budget of that year (35). The rest of the budget revenue was coming mainly from customs and monopolies. If we consider the percentage of the agricultural sector in the GNP, which was around 70 % in the importance of the tax appears more vividly (36).

The years 1925 and 1926 constituted also the beginning period of the first sales and excises in Turkey. The first sales tax was imposed in trading and services sectors. The tax rate was around 2,5 %. The tax-payment had to be made by affixing stamp or bandroll, which was an old system. In completion of

this first sales tax, in 1927, an excise on some amusement services and some other services was enacted at rates changing from 10 % to 30 %.

The introduction of the first income tax by the Republican Government took place in 1926 by the enactment of earnings tax law (Kazanç Vergisi). This tax was imposed on the earnings of both individuals and corporations. It, therefore, played the role of both personal income and corporation income taxes. The main feature of the tax, which made it seem somewhat modern was the declaration system that was adopted. Thus, the tax would be levied upon the self-declaration of the tax-payers. In the tax-return, the tax-payers were required not only to declare their net incomes, but, at the same time, they were responsible for giving information about some cost factors such as salaries and other cost elements. Hence it seems that the tax was designed to modernize the taxation system as a whole. However, some modern techniques in taxation were lacking in that tax; for example no allowance was made for minimum subsistence. The rate structure had a very mild progressivity, ranging between 6 and 14 %.

During that period some other taxes, such as gifts and inheritance taxes, etc. were employed, but their share in the budget was rather small.

Besides the earnings tax, the greatest portion of the budget revenue was provided by two important sources; one of them was the revenue gained by the state monopolies and the other was customs. In 1925, customs revenue constituted 42 % and the gains from the state monopolies 11 % of the budget (37).

As to the distribution of the taxes between direct and indirect taxes during that period, we have the following picture: The direct taxes were 32 % of the total tax revenue while the indirect taxes were about 68 % in 1925 (38).

In order to evaluate the effectiveness of the tax system as a whole, it is necessary to find the income elasticity of the

system in that period. In the year 1925, the tax elasticity was 0.7 (39). As the elasticity coefficient is less than one, the tax system can not be accepted as an efficient one. By efficiency it is meant that the tax system can play the role of a stabilizer against market fluctuations and it provides a stable revenue to the state. We have to notice that during periods of depression a tax with an elasticity coefficient less than one provides the state relatively more revenue than a tax with an elasticity coefficient of more than one. However, this factor should not be counted favourably since the first one lacks the important quality of being a stabilizer.

There was a special character of the customs duties employed in the 1930's. At that time, exports as well as imports were taxed under the same tax law. The reason for that becomes clear enough if we consider the economic and social structure of the time. The trading sector could not be reached sufficiently because of the lack of large-scale enterprises. For this reason the government tried every possible access to reach the real earnings of the citizens. Exports, along with imports, were not able to evade tax authorities. Thus, they were taxed. That the world-prices could not be affected by export taxation system made it possible for the system to be used as a means of reaching incomes of exporters. In 1927, the imports were about 14 % and the exports were about 10 % of the GNP (40). Thus, the foreign trade sector seemed attractive to the tax authorities at the time.

After having given a brief description of the main taxes employed during the very first years of the Republic, we can now go on with a general review of the period between 1930 and 1950. During that period only one tax appears to be of great importance in the field of income taxation. That tax was called the economic crisis tax (iktisadî Buhran Vergisi) and its main contribution to the revenues tax which had been enacted in 1926 was the inclusion of wages within the scope of income taxation for the first time. Almost no other important changes had taken place in that taxation area.

On the other hand, there are two other taxation areas in which we can contemplate important improvements. The first one was the enactment of a relatively modern land tax to codify the system which had hitherto been administered by various decrees. It was enacted in 1931. Another tax on buildings was later enacted and in 1935 these two taxes were brought together and the taxation authority was delegated to local authorities. Thus, in Turkey, a first step had been made towards fiscal decentralization for the first time. One important defect of those taxes was that the tax base eroded in time while the price increases took place, because the tax-amount was a percentage of the assessed value of the land or building during the first assessment. Through the inflationary periods the real value of such real estates increased tremendously without affecting the previously assessed values. This mechanism constituted one of the reasons of financial crisis of local authorities.

The most active field in taxation during that period was the area of indirect taxes: sales and excises. In 1930, a tax law was passed through the Parliament to tax sugar, both domestically produced and imported, and petroleums.

In the indirect taxation field the most important tax appeared in 1934 which was the first turnover tax in Turkey. The tax would be levied upon the declaration made by the tax-payers. The rate changed from 2,5 % to 10 %. Banking services were also included.

The introduction of such important indirect taxes during that period is natural because the domestic industry and imports were gaining importance, thus enabling the government to extend taxation possibilities to new areas. However, the exclusion of some small sized firms in the taxation led to disintegration of firms. Thus, the tax had an unexpected consequences on the integration and optimum sizes of the firms.

Still another excise tax law was enacted in 1935 to cover some other new commodities which had not been covered hitherto.

The impact of the Second World War on the Turkish taxation system was the employment of an extra-ordinary wealth tax enacted in 1942, which was called Wealth Tax (Varlık Vergisi). That tax should be levied according to the value of the wealth of the tax-payers. The value of the wealth had to be determined by local authorities. The tax-payers had no right to object to the assessed values. That tax had been employed for about one year and it was repealed in March, 1944.

To get a general view about the technical properties of the taxation system employed during that period, the below table has been introduced (41).

Table — 8
Some Technical Properties of the Taxation
System Employed Between
1930 - 1949

Selected Years	Horizontal Distribution		Tax/GNP Elasticity	Tax Burden
	Direct	Indirect		
1930	26 %	72 %	0.3	10.4
1935	44 %	56 %	1.0	11.8
1940	47 %	53 %	1.1	9.6
1945	39 %	51 %	2.7	9.5
1949	38 %	62 %	4.6	14.6

From the above table one can get an overall impression about the general characteristics of the tax system employed during the period between 1930 and 1949. The tax burden was slightly above 10 % in general, which was a very low level when the state was badly in need of financial resources to undertake some investments for economic development. But this is not a very surprising situation for Turkey during that time, because the wealthy and politically powerful pressure group, the agricultural sector, had been successful in keeping themselves outside of the scope of taxation. There were some persuasive reasons,

such as high rate of illiteracy and high compliance costs, etc. for not including that sector within the taxation field. However, a sector which was providing almost the three quarter of the GNP at the time should have been covered by taxation to boost capital accumulation in the economy.

The second property of the system employed during that period was that the relative share of indirect taxes was greater than that of direct taxes, which was a property of the taxation system that contradicted tax equity. However, the government was, in a way, obliged to resort to indirect taxes heavily, because it was the easiest way of collecting revenue. The direct taxes that had been employed then did not have sufficient progressive rate structure as to yield ample revenue.

Another aspect of the taxation system of that period was it's being somewhat a system with a relatively high income elasticity coefficient. However, one has to be cautious in interpreting this high elasticity. That high elasticity coefficient can not be attributed to the built-in-elasticity character of the taxes of that period, but it should be attributed to frequent enactment of new tax laws (*). Thus, the tax revenue, in general increased at a relatively high rate, though the revenue of a single tax might not show such a high rate of increase.

The beginning of the year 1950 was an epoch in the establishment of modern income tax system in Turkey by the advent of the Income Tax Law and the Corporation Income Tax Law.

A commission headed by Fritz Neumark prepared the draft of those laws. Though there had been many changes in both laws since then, the main bodies of the laws were kept up to the present time. One radical change in the income taxation, which was made in 1960, had been the inclusion of the agricultural

(*) In technical terms, elasticity coefficient is relevant where there is no change in tax laws.

incomes in the tax, which had not been included in the first version.

In the Turkish income taxation system individuals and corporations are treated as separate bodies subject to taxation.

In the recent version of the income taxation system seven categories of income are cited. These are business income, agricultural income wages and salaries, professional incomes, income from immobile and mobile assets, and miscellaneous incomes. Thus, almost all kinds of incomes have been covered, only leaving capital gains and windfalls aside. It had always been a leakage in the income taxation system to leave capital gains aside, though there may be some real reasons for their-exclusion it is not fair to tax capital gains at the same rates at which ordinary incomes are taxed, because capital gains may be fictitious gains and such a progressive tax may be unfair. However, in an economy of high price increases and urbanization, some part of such windfalls should have been channelled to the public sector. Up to the 1970's this vacuum had not been filled. Recently, a special tax had been enacted to fill this gap by taxing windfall gains on immobile asset.

The rate structure of the income tax is progressive, the highest marginal rate being 66 %. The progression stops at the level of 1.000.000 Turkish Liras. That amount and the amount of incomes above that figure are taxed at 60 % flat-rate.

The philosophy of progressive taxation depends on the diminishing marginal utility of increasing income, on the one hand, and the achievement of equal marginal sacrifice among tax-payers on the other hand. In order to secure those aims, the progressive structure should be effective. In the Turkish income tax system the progression is somewhat nominal, because the inflation has shifted the mass of the burden on the low-income tax-payers. Most of the high-income tax-payers can earn incomes above the 1.000.000 liras limit and pay taxes

at the flat rate of 60 %. Thus the progression can not be achieved in the real sense. In order to have an effective progression in the taxation system, either the income brackets or the tax rates should be adjusted according to the inflation. Since we are not concerned here with this subject directly, we shall not go into further details.

In the present income taxation system almost all the modern taxation techniques such as minimum allowance, allowance for dependents, withholding system, etc are being used.

The corporation income tax aims at both public and private corporations in order not to disturb the cost structures in the two sectors. However, the rates applicable to corporations in different sectors differ, 25 % being applied to the corporations in the private sector and 35 % being applied to the corporations in the public sector.

Both personal income and corporation income taxes are the main national taxes.

In 1957, a new sales tax was enacted to substitute the old sales and excise taxes. In the new sales tax indigenous products and imports are taxed.

In the indirect taxation field, another important event was the acceptance of tax-redemption system in exports. Theoretically, this system is the consequence of the destination principle in indirect taxes. Accordingly, a commodity has to bear the tax of the country in which it is consumed. To avoid double taxation, therefore, the exporting country should not levy any indirect tax on the exported commodity. However, in Turkey the tax redemption system has not been employed towards this purely theoretical end. Instead, the amount which is redeemed as indirect tax in the cost element has been calculated so high as to exceed the real amount of the indirect taxes in the commodity and cover some of the real costs. Thus, the tax redemption system has adopted the function of an export encourage-

ment measure by disguising some of the real cost of the exported commodity.

Another related subject of importance, especially in the field of local finance, has been the tendency toward centralization in the taxation system by changing the land and property taxes from being local taxes into national taxes, though some provisions have been accepted to give shares to local authorities. In that specific field of taxation, tax-base had also been altered as to be assessed every five year, thus, enabling the value increments to be reflected in that payments.

Let's now introduce some technical properties of the taxation system, employed in Turkey after 1950 (42).

Table — 9

Some Technical Properties of the Taxation System

Selected Years	Horizontal Distribution Direct	Distrubition Indirect	Tax/GNP Elasticity	Tax Burden
1950	39 %	61 %	— 2.1	11.9 %
1955	36 %	64 %	0.8	11.7 %
1960	42 %	58 %	0.3	11.0 %
1965	35 %	65 %	1.9	12.7 %
1970	38 %	62 %	1.3	15.6 %
1973	22 %	58 %	1.1	16.8 %

The distribution of taxes between direct and indirect taxes is quite poor, giving always relatively more room to indirect taxes which are regressive in character. Among many other technical reasons, the poor implementation of direct taxes and relatively administrative ease of indirect taxes have led to that situation. It would be more proper to spare more room for direct taxes in the system if equity in taxation is to be attained.

The burden can be considered relatively low in the economy, in general, it should be higher in order to provide enough

funds to the state to enable her to undertake some infra-structural investments along with regular administrative tasks. However, it should be taken into consideration that there is a close relation between the stage of economic development and the general tax burden in an economy.

4. A Comparison:

After having explained briefly the development of the taxation systems in Japan and Turkey respectively, it is now proper to make a comparison between the two systems in order to find out the favourable and detrimental effects of the systems on the functioning of the economies of two countries.

To begin with, we have to settle our model in a theoretical system. Both for Japan and Turkey the model is the capitalistic mode of production, though to call it a mixed economic system is more proper for the second. However, if we try to envisage the future, it can be safely stated that the gap between the two countries in that way may be closing. The problem of what would be the alternative of the system that those countries have hitherto employed, lies outside of the scope of this paper. In other words, the system problem has been taken as given here.

The basic similarity between the two countries is the employment of a kind of agricultural tax in both countries during the take-off period when the agriculture constituted the backbone of the economies. However, the similarity is confined only to the initial stage of the land tax in Japan and the tithe in the Ottoman Empire and the first years of the Republican Government. In the Tokugawa Era the land tax was employed, thus the agricultural sector carried most of the tax burden. The Meiji leaders revised the tax, introducing a cash payment system instead of an in-kind payment system. Thus the tax was given two functions at one time: first to shift the rural economic surplus produced in the agricultural sector to the public sector to be invested mostly in industrial areas, and, secondly, to

monetize the economy to the extent that the tax could be effective. Besides these direct impacts there was some very important consequences of the tax. The tax enforced the sale of small lands, thus giving way to the concentration in land ownership. Leaving the important problem of the distribution of wealth in society aside, it can be argued that the concentration mechanism made higher rates of savings available to the economy than it would otherwise be possible. The other side-effect was the provision of an ample and cheap labor force for industry. This second effect had, no doubt, a detrimental impact on income distribution. However, both the effects and side-effects were, perhaps, required for purposes of capital accumulation, though they had undesirable effects on income and wealth distribution.

As to the situation of the taxation of agriculture in Turkey, the development had been somewhat discouraging. The main agricultural tax, the tithe, had been very poorly administered in the Empire period. The Republican Government had abolished it totally in 1925 without introducing any substitute. The second tax on agriculture, the land tax, had also been poorly administered by decrees. The assessment method of that tax prevented it from providing a high yield to the state. However, the situation during the 1925 crisis should be excluded from the analysis. It was necessary to wait until the 1960's for the inclusion of the agricultural sector systematically in the taxation system though it is still not taxed effectively. Thus, the main field of economic activity had been out of the scope of effective taxation.

Among the reasons for the abolishment of the tithe, the poor administration was the most important one. But it does not seem very plausible to repeal a tax on the most important sector of the economy totally for a reason which can be corrected just by altering the assessment and administration methods. Therefore, we have to search for another more sound reason for such an important political decision. Such a reason can be found in the economic and political power and influence

of the agricultural sector upon the government which ought to depend on a social class in strengthening her position against both foreign and domestic opposition powers. For this reason, along with the detrimental effects for the 1929 crisis and the Second World War, the exclusion of the agricultural sector from the scope of taxation had been an important handicap in the way of capital accumulation.

In the field of income taxation in the modern sense, it was necessary to wait until 1950 for Turkey, though it had been effective in Japan as early as 1887. Therefore, Japan had advantages in developing administrative skills in tax administration. The administrative ease had also been achieved by the establishment of large-scale industries and the adoption of western techniques earlier than they have taken place in Turkey.

In Turkey various direct taxes had been effective before the enactment of the Income Tax Law in 1950, but they had been ineffective in the provision of a high yield to the public sector.

The overall success of the systems can be evaluated also from another viewpoint. That is the percentage of tax revenue in the GNP. This ratio is of great importance, because it shows the relative degree of opportunities available to the public sector without resorting to the deficit financing method. In Turkey, throughout the Republican period, the tax burden on the economy has never been more than 20 %, the rate which Japan had attained during the early periods of the Meiji Era. In the initial stage of the economic development process, the high percentage of taxes in the GNP provides high rates of savings for infra-structural undertakings. In Turkey that rate had hardly reached 10 % in the period between 1923 and 1960. This is a very low rate for capital accumulation in the public sector.

Finally, we have to make a comparison from the viewpoint of tax-equity between the systems which have been employed in the two countries. To serve this purpose we have to bring the relative shares of direct and indirect taxes into focus.

In Turkey the picture is as follows. From the very beginning year of the Republic to the present the relative share of direct taxes which are considered to be more equitable in comparison with indirect taxes has always been less than 50 %, sometimes going down as far as 30 %. If the poor implementation of the direct taxes are taken into consideration, the general outcome of the equity aspect of the taxation system in Turkey becomes more discouraging.

As for Japan, it is seen that the relative weight of direct taxes has been more than 50 % for most of the time. This rate had reached 60 % after the 1950 revision had been made in accordance with Shoup Mission recommendations.

In a taxation system, no doubt, there are certain functions for indirect taxes as well as for direct taxes. However, with certain reservations, when the equity aspect is taken into consideration, direct taxes gain the utmost importance. It is the direct taxation system which can be tailored best to the taxable capacity of the tax payer. Certain measures can be taken in the field of indirect taxation to fit those taxes to the taxable capacity of the individuals, but a complete success in that way is unattainable. Therefore, it is proper to confine the scope of the indirect taxation field only to their economic functions, such as curtailing of demand for certain goods, covering of external costs, etc., and resort to direct taxes for purely revenue purposes.

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