1. When establishing the Working Party on Border Tax Adjustments the Council authorized the secretariat to approach the OECD to obtain documentation arising from the detailed work already undertaken in that organization.

2. The Secretary-General of the OECD has informed the Director-General that certain classified documentation has been released "for the internal use of the Working Party of the GATT". This is reproduced in the annexes to this document, which is being distributed to members of the Working Party only.

Annex A:

Border Tax Adjustments applied by member countries to exports and imports. Note dated 27 January 1965 (OECD document CES/65.3).

Annex B:

Annex A

BORDER TAX ADJUSTMENTS
APPLIED BY MEMBER COUNTRIES TO EXPORTS AND IMPORTS

(Note by the Secretary of the Council)

27 January 1965
(CES/65.08)

I. SUMMARY OF CONCLUSIONS OF A SYMPOSIUM ON BORDER TAX ADJUSTMENTS ORGANIZED BY THE SECRETARIAT ON 17-19 SEPTEMBER 1964

1. A Symposium of economists and fiscal experts were invited by the Secretary-General to discuss the economic rationale and the effect on international trade of border tax adjustments as they are at present applied. The participants were:

- Professor R. COOPER, Yale University.
- Professor F. FORTE, Turin University.
- Professor K. HAUSER, Frankfurt University.
- Professor R. MUSGRAVE, Princeton University.
- Professor L. MUTEN, Uppsala University.
- Professor A.J. VAN DEN TEMPEL, Amsterdam University.

The main conclusions of the Symposium are summarized below.

A. INDIRECT TAXES

2. In practice, indirect taxes are not fully shifted into product prices, whether this is due to a fall in factor prices or to tax evasion or other causes.

3. In practice, selective excises on goods with relatively inelastic demand are likely to be shifted to a greater extent into product prices. With general taxes of wide coverage and uniform rates, the effect on absolute prices as well as on relative prices is likely to be least.

4. In the absence of border adjustments for indirect taxes, the shifting of indirect taxes would be particularly difficult for countries whose prices are closely linked to world prices, because of their heavy reliance on international trade. Disallowance of some border tax adjustment for indirect taxes in such countries would reduce their freedom of choice between various possible tax structures and techniques of indirect taxation and of pursuing economic and equity objectives, including the use of tax policy for economic growth.
B. DIRECT TAXES AND SOCIAL SECURITY

5. Certain direct taxes, and particularly the corporation profits tax, may be partially shifted into product prices although the degree of shifting may vary from country to country.

6. Of the direct taxes, corporation profits taxes would appear to have one of the best cases for being made eligible for border tax adjustments; but if they were made eligible, this might have little effect on the existing situation in term of balance of trade advantage, since adjustments would be made by all countries and rate differentials are slight. However, if shifting conditions or export coverage of the tax differ between countries, this result might not hold.

7. Payroll taxes and social security payments are also likely to have some effect on product prices.

C. GENERAL

8. "Neutrality" can take on two meanings in a discussion of the impact of taxes on foreign trade. It can refer to the effect of tax changes on the balance of trade under a régime of fixed exchange rates, or it can refer to the effect on the level and commodity composition of trade in a régime in which monetary or exchange rate adjustments ensure trade balance.

9. Under fixed exchange rates, the existing situation regarding eligibility for border tax adjustments would neutralize the effects of tax changes on balance of trade only if indirect taxes were reflected fully in a rise in product prices and if direct taxes were not shifted into product prices. This disregards any effects of government expenditure on export costs.

10. Without the more tentative conclusions at 5 and 7 above, it still follows from the fact that indirect taxes are not fully reflected in an increase in product prices that full border adjustments for indirect taxes are not neutral in their effect on balance of trade. An increase in indirect taxes with full border tax adjustments would therefore be favourable from the point of view of balance of trade, to the extent that the increase in taxes is not fully reflected in prices.

11. Despite the conclusion in paragraph 10 above, most of the participants felt that the alternatives of making either indirect taxes ineligible, or direct taxes eligible for border tax adjustments would be unlikely to produce a more neutral situation and would be open to many other difficulties.
12. In a situation of flexible exchange rates, no balance of trade problem arises, but if neutrality is interpreted in the efficiency of resource allocation sense, the existing situation would be strictly neutral only if the initial exchange rates reflected an equilibrium rate in a perfectly competitive world. The problem of neutral rules under such conditions was not, however, pursued.

13. Other relevant questions not pursued include the effect of border tax adjustments practice on national tax systems and on capital movements and what are the appropriate criteria for distinguishing between "direct" and "indirect" taxes for the purpose of border tax adjustments.

D. EFFECTS OF FUTURE TAX CHANGES UNDER DISCUSSION

14. An evaluation of the effects of the possible changes under discussion in the indirect taxation of certain European countries did not involve most of the analytical difficulties referred to above, since in the main one form of indirect taxation was being substituted for another. These changes, which would result in balance-of-trade advantages if border tax adjustments were made in full, could be analyzed as follows:

(a) In the cascade countries, the substitution of a value added tax would result in an increase in border tax adjustments relative to home burden because, under the method used in computing border tax adjustments in the cascade systems, the home burden is not fully compensated. (This would clearly improve balance-of-trade conditions.)

(b) A switch from a retail sales tax including investment goods and a tax on energy (which taxes are not refunded on exports) to a value added tax excluding investment goods and energy and with a higher rate on consumption goods (which would be refunded on exports), would increase border tax adjustments. (This would clearly improve balance-of-trade conditions.)

(c) In the cascade systems, a switch from a tax including investment and consumption goods (which tax is not fully refunded on exports) to a value added tax excluding investment goods and with a higher rate on consumption goods (which would be fully refunded on exports), would increase border tax adjustments. (The balance-of-trade effects would be less clear.)

(d) The combination of an increase in indirect taxation with reliefs in direct taxation or social security charges or with an increase in welfare allowances would increase border tax adjustments. (The balance-of-trade effects too would be less clear.)
II. NOTE BY THE SECRETARIAT ON THE ECONOMIC RATIONALE AND OF THE EFFECTS ON INTERNATIONAL TRADE OF BORDER TAX ADJUSTMENTS

1. The remarks in paragraphs 97-100 of the fact-finding report C(64)137 raise questions on the economic rationale of the present situation under which border adjustments are made for certain indirect taxes but not for direct taxes (or social security payments) and also on the effect of the existing situation on international trade. The following paragraphs summarize the economic arguments for and against the existing situation and consider its effects on international trade. The conclusions drawn are necessarily tentative but may serve as a basis for further consideration of these questions.

A. ECONOMIC RATIONALE OF EXISTING SITUATION

Arguments for existing situation

2. The following arguments have been put forward in favour of the view that indirect taxes should be eligible for border adjustments.

(a) The only practical way of taxing consumption is to do so regardless of the origin of the goods and this implies making border tax adjustments on imports. In addition, consumers in foreign countries should not bear a tax levied by another country and this involves making border tax adjustments on exports.

(b) Without border tax adjustments, countries relying heavily on international trade and the price of whose products is determined by world markets, would lack freedom to tax consumption since the tax could not be shifted into export prices. Similarly, without an equalization tax on imports, the domestic product might be outpriced on the home market by foreign products.

3. The following arguments have been put forward on the undesirability of making direct taxes eligible for border adjustments.

(a) In practice, it seems possible that direct taxes are not taken into account in fixing export prices.

(b) The impact of corporation profits taxes is sometimes mitigated by accelerated depreciation allowances and other fiscal measures, and even where this is not so, it is difficult to determine the real burden of the tax. If such taxes were eligible for rebate, there would therefore be the risk of disguised subsidies.

4. The following claims have been put forward on the basis of the difference between direct and indirect taxes.
(a) Even if not entirely shifted into product prices, indirect taxes are shifted to a much greater extent than direct taxes.

(b) Even if not entirely neutral, the existing situation distorts trade less than would the alternatives of making direct taxes eligible or indirect taxes ineligible for border adjustments.

Arguments against existing situation

5. It is contended that under fixed exchange rates, the existing situation would be neutral as regards international trade, only if indirect taxes were fully shifted into product prices and direct taxes were not shifted at all into product prices.

6. On this question, it is claimed that:

(a) Indirect taxes are not fully shifted forward so that to give a full rebate amounts to giving a subsidy to the extent that the tax is not shifted. Similarly, the imposition of a full equalization tax on imports amounts to an additional customs duty.

(b) Direct taxes, and in particular corporation profits taxes, are sometimes shifted forward and may have as much effect on product prices as a general indirect tax at a uniform rate, which is reflected in the general price level of the economy rather than in the relative price of individual products.

Evaluation

7. Much of the argument on the economic rationale of the present position hinges on the question of price shifting of direct and indirect taxes. On this question, the following points appear to be generally accepted among economists:

(a) Indirect taxes are not fully shifted into price of goods, but to some extent they are absorbed in factor costs. Evasion of indirect taxes may also be a relevant factor. In practice, specific excises are more likely to be shifted forward than general indirect taxes at uniform rates, which accounts for the fact that criticism of the existing position is not generally directed at excises.

(b) While not fully shifted forward, indirect taxes are usually shifted to a much greater degree than direct taxes.

(c) Of the direct taxes, it is corporation profits taxes that are most likely to be shifted forward. This forward shifting may vary from country to country. It is unlikely that the balance of trade would be greatly affected if profits taxes became generally eligible for
border tax adjustments, since there is not much difference between rates of profits taxes in different countries, but this variation in price shifting makes forecasting of the effects difficult.

3. It also appears to be generally accepted that while not entirely neutral, the existing situation has more to commend it than unlimited eligibility for direct taxes for border adjustments or complete withdrawal of eligibility for indirect taxes. Even if a more neutral rule could be devised, it would be very complicated to formulate and very difficult to apply.

B. EFFECTS ON INTERNATIONAL TRADE

9. In a situation of fixed exchange rates, full border adjustments for indirect taxes would appear to confer a balance-of-trade advantage to the extent that the taxes are not fully shifted into the prices of goods. At present, most countries make something near full border adjustments, but any balance-of-trade advantage given to countries with greater reliance on indirect taxes may have been offset in the past by changes in exchange rates, general price levels and other factors.

10. Increases in border tax adjustments may occur in the following ways:

(a) through a change within a cascade system because it has been discovered that border adjustments are less than the tax burden on the home market;

(b) through a change from a cascade system where border adjustments do not fully compensate for the home tax burden to a single stage or T.V.A. system where they approximately reflect the home burden;

(c) through a change from a tax which includes investment goods to a tax producing an equivalent yield, but which excludes investment goods and therefore requires a higher rate on other goods;

(d) through the substitution of an indirect tax for a direct tax;

(e) through an increase in rate or coverage of indirect taxes.

11. It seems fairly clear that increases in border adjustments arising from (a), (b) and (c) above would have some export-promoting and import-inhibiting effects. There would of course be a deterioration in the terms of trade of the countries concerned and the ultimate effects on their balance of trade would depend on export and import elasticities. The effects of increases in border adjustments arising from (d) or (e) are less clear because the secondary effects on domestic wages and prices may countervail any advantage in balance of trade.

12. The possible impending changes in Europe discussed in paragraphs 92 et seq. of the fact-finding report provide examples of changes of the kind described under (a), (b) and (c), but as remarked in paragraph 94, they are being considered by countries who make least border adjustments in relation to the internal indirect tax burden.
I. MANDATE

1. The Working Party on Border Tax Adjustments, which was set up by the Council on 13 April 1965 (C/M(65)8 of 29 April 1965) and the composition of which was decided on 29 April 1965 (C/M(65)9 of 24 May 1965), was given the following mandate:

(a) To consider the information contained, and any problems raised in C(64)137 and CES/65.08, in particular the economic, fiscal and trade aspects of the present border tax adjustment practices.

(b) To examine the economic policy implications of any problems raised and to report to the Council after having consulted the competent bodies of the organization, in particular the Fiscal and Trade Committees.

(c) The Working Party should consider in particular whether a notification procedure or a prior consultation procedure should be envisaged within the OECD with regard to changes Member countries contemplate making to their systems of indirect taxation and border tax adjustments. It should also consider whether a confrontation procedure on border tax adjustments applied by OECD Member countries should be envisaged and whether any attempt should be made to move towards greater similarity in the systems applied in the different Member countries.

2. The Working Party has held seven sessions on 26 May, 2 July, 20 September, 8 December 1965, 3-4 February, 2-3 March and 17 May 1966. In addition to the members of the Working Party (France, Germany, Japan, Netherlands, Sweden, Switzerland, United Kingdom, United States, Commission of the EEC), representatives of Belgium, Canada, Denmark, Greece, Ireland, Italy, Norway, Spain, Turkey and of the European Coal and Steel Community have also attended the meetings. The
Working Party has considered papers by representatives of the United States, Germany, the EEC Commission, the United Kingdom and France primarily dealing with the question of tax shifting, a general paper by the Chairman and a paper on recent developments on border tax adjustments by the secretariat.

3. Having regard to the fact that this report is already presented later than was intended, the Working Party thought that the Council would prefer to receive the report at this stage rather than that its presentation should be delayed further for consultation with the Fiscal Committee and the Trade Committee, particularly in view of the limited nature of the recommendations in the report. These Committees are being asked to comment on this report at their next session and the Working Party considered that it should be left to the Council to decide whether or not to discuss the report before these comments are received.

II. PROBLEMS

4. Discussion in the Working Party has concentrated on the trade effects of the present international practices under which certain indirect taxes are considered eligible for border adjustments* while direct taxes and other taxes such as payroll taxes, social security taxes and property taxes are not generally regarded as eligible.

5. The problems in regard to trade effects fall into three classes:

(a) The effect of existing tax structures and border tax adjustments on international trade.

(b) The effect of changes in indirect taxation and border tax adjustments on international trade.

(c) Special questions:

(i) Cascade systems;

(ii) "Taxes occultes";

(iii) Excise duties.

The effect of existing tax structures and border tax adjustments on international trade

6. Most delegates were of the opinion that the question whether or not the existing system of border tax adjustments conferred a trade advantage on countries relying to a greater extent than others for their revenue on taxes eligible for border tax adjustments depended primarily upon how taxes were shifted into the prices of goods.

*Border tax adjustments are regarded as covering the indirect taxes (including excise duties) remitted on exported goods (i.e. never paid either as a result of administrative arrangements or because the goods are not chargeable at the time of exportation) as well as the indirect taxes rebated on exported goods; they also cover indirect taxes on imported goods whether levied at the frontier or subsequently.
7. It was generally agreed that if taxes eligible for border tax adjustments were fully shifted into prices and taxes ineligible for border tax adjustments were not shifted into prices at all, the existing system would be neutral in its effect on trade. If, on the other hand, eligible taxes were less than fully shifted into prices or ineligible taxes were shifted into prices to some extent, it was accepted by most delegates that the system would not normally be neutral. Consequently, the Working Party discussed in detail the problem of tax shifting and a number of papers were submitted by delegates on this question. As the question of shifting raises complicated issues of economic analysis, empirical evidence and business psychology it is not proposed to go into the details of the argumentation in this report, but only to summarize the conclusions of the Working Party.

8. Some delegates, including the delegate for the United States, were of the opinion that in most cases, indirect taxes regarded as eligible for border adjustment were not fully shifted into prices and that consequently full border adjustments for such taxes often had the effect of a subsidy on exports and of a duty on imports. Other delegates, including the delegates for France and the United Kingdom, were of the opinion that such indirect taxes were normally shifted into prices, either in full or approximately so.

9. There was general agreement that of the direct taxes, corporation taxes are likely to have some effect on prices, though the view of some delegates that the effect was likely to be substantial was not shared by the other delegates.

10. The delegate for the United States also questioned the logic of making border adjustments for taxes but not for government expenditure since the firms producing the articles on which the adjustments are made may benefit substantially from the proceeds of taxation through, for example, government subsidized internal transport systems or governmental contributions to employees' welfare, part of the cost of which would otherwise fall on the firms concerned. While accepting this might be so, some other delegates doubted whether the impact on prices of such cost-reducing services would be large.

11. As a consequence of these divergent views on tax shifting and on the importance of cost-reducing government expenditure, the Working Party was unable to reach unanimity on whether the existing system of border tax adjustments necessarily favoured countries relying to a greater extent than others for their revenue on taxes regarded as eligible. Those delegates who considered that present border tax adjustment practices gave certain countries an advantage in international trade, agreed that this advantage over a period may have been counterbalanced by changes in exchange rates, general price levels and other factors, and were therefore primarily concerned with future changes in border tax adjustments.
The effects of changes in indirect taxation and border tax adjustments on international trade

12. Changes in internal taxation may in some circumstances affect international trade. One obvious case is the fact that a general increase in taxation levels, as part of a domestic anti-inflationary policy, would be likely to reduce home demand, so lowering the level of imports and enabling domestic resources to be made available for additional export production. Conversely, a lowering of taxes for economic growth purposes is likely to be balance-of-trade disadvantageous. These effects, however, are not the concern of the Working Party as they do not relate particularly to the question of border tax adjustments.

13. On the other hand, the balance of trade of a country may be affected by changes in border tax adjustments whether or not resulting from modifications in domestic taxation. For example, a country operating a cascade tax might increase border tax adjustments without changing domestic levels of taxation because previous border adjustments did not fully compensate for the internal tax burden. Even in this case, such increases in border tax adjustments would be likely to have an effect on international trade.

14. Similarly, a country which had been obtaining revenue by such taxes as a payroll tax, a social security tax or an industrial property tax, all of which are generally regarded as ineligible for border adjustments, might substitute a tax regarded as eligible, in which case it would seem likely that the effect would be balance-of-trade favourable. Or if a country operating a cascade system in which the overall domestic burden was not fully compensated by border adjustments switched to a single-stage or a value-added tax where the burden was fully compensated, there would again be an improvement in its competitive position. A number of the changes recently undertaken or contemplated by Member countries are of the kind described in this and the preceding paragraph, so that the problem cannot be regarded as theoretical.

15. Despite therefore its inability to agree on the extent of tax shifting or on the degree to which the existing system of border tax adjustments might be regarded as neutral in respect of international trade, the Working Party was able to agree on the fact that changes in indirect taxation and their associated border tax adjustments could have effects on international trade and on a country's competitive ability and that those effects would become more important if present tariff barriers to trade were reduced.

16. The Working Party felt that the possibility of such tax changes and their effects on international trade might be regarded from two different points of view. In the first place the fact that changes in indirect taxation could affect a country's ability to compete in the international market and therefore its balance of payments might be considered in the context of the study of the adjustment process and of the study on the use of fiscal policy now under progress in other parts of the organization under the aegis of the Economic Policy.
Committee. On the other hand, the possible international trade effects of changes in indirect taxation or border tax adjustments may also be of concern to the trading partners of the countries making such changes, and the Working Party's terms of reference required it to consider whether any international action is required to meet such concern. This question is dealt with later in this report.

Cascade systems

17. Criticism has been voiced against the adjustments made by a number of countries in respect of cascade taxes. While such indirect taxes enter into costs of production and are carried forward into final prices in much the same way as single-stage or value-added taxes, their incident on any particular article can only be calculated as a rough average. In practice therefore full adjustment based on such averages is likely to result in import equalization taxes being too high vis-à-vis some domestic goods and in certain articles or certain firms receiving export subsidies. On the other hand, averaging also involves under-compensation and it is claimed that countries applying cascade tax systems normally keep their rates of export rebates and import equalization taxes on the low side in order to prevent over-compensation.

"Taxes occultes"

18. For reasons similar to those mentioned in the preceding paragraph, criticism has also been voiced against the practice of applying border adjustments for "taxes occultes" (i.e. the taxes on capital goods, auxiliary materials and services used in the production of goods) even though the economic justification for making such adjustments is not essentially different from that for making border adjustments for indirect taxes on the goods themselves. Until recently border tax adjustments for "taxes occultes" were confined to countries operating cascade systems.

19. In this context, there was some feeling that the recent United Kingdom export rebate scheme might become an undesirable precedent in that it was the first time that border tax adjustments were being made for "taxes occultes" in respect of (a) a single-stage tax, (b) an excise duty, or (c) taxes such as the vehicle licence duty. The delegate for the United Kingdom considered that these differences between United Kingdom practice and practices in certain other countries were essentially not differences of substance, but differences of form. Some other delegates considered that the United Kingdom scheme constituted a difference of substance as well as form and that there was a possibility that other countries might follow this example and make border tax adjustments for production costs arising from similar "taxes occultes" or even from other taxes. There would thus be a danger of continued extension in border tax adjustments practices.
Excise duties

20. There has been no criticism of the principle* of present border tax adjustment practices with regard to such traditional excises as those on tobacco, alcohol and hydro-carbon oils. Two features distinguish these from most other indirect taxes. First, the rate of tax is usually very heavy in relation to the value of the commodity. Secondly, the demand for these commodities is relatively inelastic. For these reasons some delegates, who took the view that consumption taxes were not fully shifted into prices, considered that the traditional excise taxes were more likely to be fully shifted than may be the case with general taxes levied at a much lower rate over a wide range of commodities.

III. POSSIBLE FUTURE ACTION

21. The Working Party discussed the following methods of dealing with the problem of possible disturbances in trading patterns arising from changes in border tax adjustment practices:

   (a) Greater similarity of tax systems of Member countries.

   (b) Changes in present border tax adjustment practices.

   (c) A notification procedure.

   (d) A consultation procedure.

   (e) A confrontation procedure.

Greater similarity of tax systems

22. While some delegates felt that a perfect solution might be found in the long run only through the harmonization of tax systems of all the OECD Member countries, the Working Party was in agreement that this was unlikely to be achieved in the foreseeable future. Such factors as the preservation of fiscal autonomy and the diversity of political, social, historical and economic factors in Member countries were likely to continue to be reflected in divergent tax structures. The Working Party did not feel that at this stage it would be profitable to consider steps designed to lead to greater harmonization of tax systems.

*Attention has been drawn to instances where the excise on imported goods exceeds the excise on similar home produced goods.
Changes in present border tax adjustments practices

23. Various suggestions were made in the Working Party for modifications to the present border tax adjustment practices including the gradual abolition of border tax adjustments, other than those in respect of traditional excises, a standstill on increases in adjustments, and the placing of a ceiling on the total of such adjustments which any country might make. On the other hand, it was suggested that the Working Party should discuss whether border tax adjustments might be permitted in respect of taxes such as corporation profit taxes, which are at present ineligible.

24. The Working Party did not however discuss these proposals in detail since it became clear that a majority of the members were not persuaded that any of the changes proposed would effect such an improvement in present practices as to warrant the very serious political and practical difficulties which their introduction would cause. The Working Party therefore concentrated on the question of the establishment of procedures for notification, consultation and confrontation referred to in its mandate.

Notification procedure

25. The Working Party considered that a notification procedure might serve two purposes. In the first place it would serve to keep Member countries informed about actual and contemplated changes in the border tax adjustments of other Member countries and provide material for periodic reviews of developments. Secondly, it would provide information upon which a consultation procedure might be based.

26. The establishment of a notification procedure would give rise to two main questions. First, there is the problem of defining the range of changes in border tax adjustments of Member countries which should be notified. Secondly, there is the question of the timing of notification, which includes both the question of when Member countries should notify the organization of such changes and when the organization should disseminate this information to other Member countries.

27. As regards the kinds of changes which should be notified, the Working Party found it difficult to give an exhaustive list. It was felt, however, that if a notification procedure were to be set up, the following kinds of change should be notified:

(a) Changes in border tax adjustments arising from changes in tax systems (e.g. the substitution of one form of tax for another as is proposed in Denmark and Germany);

(b) Changes in border tax adjustments arising from changes in either (i) the principles or (ii) the practices applied to them, but in both cases not resulting from changes in domestic taxation (e.g. (i) the recent export rebates introduced into the United Kingdom and (ii) the recent export rebates introduced for particular products in Belgium);
(c) Changes in border tax adjustments arising from changes in rates of indirect taxation on goods which represent a significant proportion of the total value of imports or exports of the country concerned.

28. As regards the time when changes should be notified to the organization, those changes of systems or principles described in paragraph 27(a) and 27(b)(i) are usually publicized well in advance (e.g. the proposed value-added taxes in Denmark and Germany); they may involve in the first place the setting up of a committee of enquiry, secondly, a decision in principle by the government to adopt them and finally, detailed legislative proposals being put forward to parliament. The Working Party felt that it would be difficult to lay down general principles of universal application as regard the stage or stages at which changes of this kind should be notified, particularly as in certain cases governments might be reluctant to notify them before they had been submitted to parliament. There was also the difficulty that the proposed changes might undergo considerable revision during their passage through parliament. On the other hand, the Working Party considered that governments should bear in mind the desirability of notifying contemplated changes of this kind as early as possible in order to ensure in particular that the views of the other Member countries concerning the impact of the change on international trade should receive as much consideration as possible. The Working Party therefore considered that changes of this kind should be notified no later than the time at which they were made known publicly by the government concerned.

29. The timing of notification of changes in rates of border tax adjustment of the kind described in paragraph 27(b)(ii) and 27(c) raised rather different considerations. In the first place, some delegates stressed that some of these changes had to be kept secret until they came into effect because prior knowledge of them would confer substantial benefits to private persons. Some delegates also stated that in their country legal provisions prevented the dissemination of information on fiscal changes before they were made known to the public. In addition, there was the technical problem mentioned in paragraph 28 above, that proposed changes might undergo considerable revision during their passage through parliament, so that it would make a notification procedure extremely cumbersome if each revision had to be notified separately. For these reasons the Working Party was agreed that while proposals for changes in taxation or border tax adjustments of the kind described in paragraph 27(b)(ii) and 27(c) should be notified to the organization as soon as possible once they were in a definite form, this was normally unlikely to be before they were made known to the public in the country concerned and in some cases not until they came into effect.

30. As regards the time when details of changes should be disseminated by the organization to the other Member countries the Working Party considered that an unjustifiable amount of work would be created if the secretariat informed Member countries each time a change of the kind described in paragraph 27(b)(ii)
and 27(c) was notified. In general it was felt that it would be sufficient if the secretariat issued a summary of such changes at periodic intervals, particularly as other delegations would normally be informed about such changes through other sources and could obtain more information from the secretariat if they were interested. In respect, however, of more far-reaching changes of the kind described in paragraph 27(a) and 27(b)(i) above, the secretariat should inform Member countries as soon as practicable after they had been notified.

Consultation procedure

31. The establishment of a consultation procedure would give rise to the following questions:

(a) What should be the subject-matter of the consultation?
(b) At what stage should consultation take place - in particular before or after the change was put into effect - and what form should it take?
(c) How should the consultation procedure be brought into effect?
(d) In what body in the OECD should consultation take place?

32. As regards the subject-matter of consultation, the Working Party agreed that it should be confined to the general international trade and payment effects of changes in border tax adjustments whether or not such changes resulted from modifications in domestic taxation. Thus, the domestic reasons for changes in taxation would be outside the scope of any consultation procedure. With regard to the international trade and payment effects, consultation would concentrate on the general policy implications.

33. The question of the timing of any consultation raised difficult issues. Some delegates felt that consultation should wherever possible take place before changes in border tax adjustments were put into effect so that views of governments who felt that they would be adversely affected by the proposed change could be fully taken into account by the government proposing the change. Other delegates stressed the sensitivity of consultation on matters relating to fiscal policy which was generally regarded as a domestic issue. In some countries there would be particular difficulty in discussing measures at the time when they were under consideration in national parliaments.

34. The Working Party was informed by some delegates that, because of the difficulties mentioned in the preceding paragraph, their governments in participating in a given case of consultation about proposed changes might feel themselves obliged by constitutional requirements or political or other important factors to limit somewhat the discussions into which they could enter if the consultation took place at an early stage. Nevertheless, the Working Party
agreed that despite these possible limitations it would be desirable to set up, on an experimental basis in the first instance and for a period of perhaps two years, a system under which, whenever possible, prior consultation would take place if one or more Member countries requested it. In some cases, also, it seemed possible that a country contemplating a change in taxation might offer consultation in its own initiative.

35. Although not strictly within its mandate, the Working Party considered that it might be helpful to the Council if it gave some preliminary consideration as to which body within the OECD should be responsible for carrying out the consultation procedure. As the consultation was to be concerned mainly with the general trade effects of changes in border tax adjustments, the Working Party considered that the Trade Committee with adequate representation of fiscal experts would be the most appropriate body to organize the consultation procedure. Such consultation might best be conducted by an ad hoc group of the Trade Committee.

Confrontation procedure

36. As regards confrontation, a factual study of border tax adjustments was undertaken by the secretariat before the present Working Party was established //C(64)137 - Parts I and II of 12 October 1964//. This has since been supplemented by a Corrigendum and by an Addendum on the British Export Rebate Scheme as well as the paper on Developments on Border Tax Adjustments referred to in paragraph 2. Action of this kind could be continued by the revision (and possibly derestriction or publication) of the study with the issue of periodic supplements to keep it up to date.

37. Unless and until more elaborate rules are established as to what is or is not permissible with regard to border tax adjustments, it seems difficult to take action of this type further than a periodical re-examination of the facts. If, however, general guidelines were generally acceptable, the extent to which individual countries' practices complied with the spirit and intention of the guidelines might be the subject of a confrontation procedure. At present, however, this is not the case. While, for example, a number of delegates felt it was undesirable to make border adjustments in respect of "taxes occultes", this view was not endorsed by those countries at present making such adjustments. In present circumstances, therefore, it would seem that action of this type will have to be confined to the dissemination of factual information and general examination of the situation from time to time.

IV. SUMMARY AND CONCLUSIONS

38. Primarily because of the diverging views of delegates on the nature and extent of tax shifting, the Working Party was unable to agree on whether or not existing border tax adjustment practices placed some countries at a competitive disadvantage as regards international trade (paragraphs 6-11).
39. The Working Party agreed, however, that certain types of changes in border tax adjustments, whether or not resulting from changes in internal taxation, could affect international trading positions (paragraphs 12-16).

40. Some delegates criticized the effects of averaging in making border adjustments in respect of cascade taxes and "taxes occultes", and considered that the introduction of border adjustments for "taxes occultes" (as in the case of the recent British export rebate scheme) increased the danger of extension of border tax adjustments, since many countries did not at present make border adjustments for "taxes occultes". On the other hand, the Working Party considered that border adjustments for such traditional excise taxes as those on tobacco, alcohol and hydrocarbon oils created no difficulties in principle (paragraphs 17-20).

41. The Working Party did not consider that the problem of the trade effects of border tax adjustments was likely to be resolved in the foreseeable future by greater harmonization of tax systems of all Member countries; nor did the majority of its members feel that at this stage there was a sufficiently strong case for modifying existing border tax adjustment practices (paragraphs 22-24).

42. In the circumstances, the Working Party recommends that a notification procedure should be established with the dual object of providing the organization with information on changes in taxation and border tax adjustments in Member countries, and of enabling such information to serve as a basis for a consultation procedure. Notification should apply to changes of the kind referred to in paragraph 27 and should take place no later than the time at which they are made known publicly by the government concerned (paragraphs 25-30).

43. The Working Party also recommends that a consultation procedure of the following kind should be established on an experimental basis and for a period of two years (paragraphs 31-34):

(a) its subject matter should be confined to the general trade and payment effects of changes in border tax adjustments and their policy implications;

(b) when requested by one or more Member countries, consultation should, whenever possible, take place before the change came into effect, even if in some cases this meant reducing somewhat the scope of consultation.

44. The Working Party considered that the Trade Committee with adequate representation of fiscal experts would be the most appropriate body to organize the consultation procedure (paragraph 35).

45. The Working Party considered that, as regards confrontation, action would at present have to be confined to the bringing up to date of the Secretariat's fact-finding report, together with a general examination of the situation from time to time (paragraphs 36-37).